164

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1941

No. 757

PRUDENCE REALIZATION CORPORATION,
PETITIONER,

vs.

A. JOSEPH GEIST, TRUSTEE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED NOVEMBER 24, 1941.

CERTIORARI GRANTED JANUARY 5, 1942.

SUPREME COURT OF THE UNITED STATES

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INDEX.

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., JANUARY 26, 1942.

[fol. 1]

IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

In Consolidated Proceedings for Reorganization under Section 77B of the Bankruptcy Act

Nos. 27496 and 27028

In the Matter of THE PRUDENCE COMPANY, INC., Debtor

In the Matter of AMALGAMATED PROPERTIES, INC., Debtor

In the Matter of a Plan of Reorganization of AMALGAMATED PROPERTIES, INC., Debtor, in Respect of the Zo-Gale First Mortgage Participation Certificates

PRUDENCE REALIZATION CORPORATION, Appellant

A. JOSEPH GEIST, Trustee, Appellee

STATEMENT UNDER RULE 13

This proceeding was commenced on May 13, 1940, by the service on Prudence Realization Corporation of the petition of A. Joseph Geist as trustee for an order declaring that the interest of Prudence Realization Corporation in and to the outstanding certificates in the sum of $818.67 and in and to the unissued certificates in the principal amount of $7,200 of the Zo-Gale Realty Co. Issue is subject and subordinate to the certificates issued by Prudence-Bonds [fol. 2] Corporation, guaranteed by The Prudence Company, Inc., and held by the general public, and that payments of principal and interest on the certificates issued and unissued held by Prudence Realization Corporation should be deferred until the certificate holders have been paid in full the principal and interest guaranteed them under their certificates, and for such other and further relief as to the Court may seem proper.

The only parties who have appeared or taken any part in the proceeding are A. Joseph Geist, as trustee, petitioner, and Prudence Realization Corporation, the respondent.

The answering affidavit of William T. Colwin, as President of Prudence Realization Corporation, was filed on

September 26, 1940, and the replying affidavit of A. Joseph Geist, as trustee, was filed on October 23, 1940.

On January 25, 1941, Hon. Grover M. Moscowitz, United States District Judge, handed down a decision granting the petition, and on January 30, 1941, made and entered an order declaring the interest of Prudence Realization Corporation in and to the issued and unissued certificates of the Zo-Gale Realty Co. Issue subordinate to the interest of third party certificate holders, and determining that Prudence Realization Corporation is not entitled to any distribution of principal or interest out of the trust estate on account of its certificates until third party certificate holders have been paid in full the principal and interest guaranteed under their certificates.

A notice of appeal from the order of January 30, 1941, was dated and filed in the office of the Clerk of the United States District Court for the Eastern District of New York on February 13, 1941.

[fol. 3] In United States District Court, Eastern District of New York

In Consolidated Proceedings for Reorganization under Section 77B of the Bankruptcy Act

Nos. 27496 and 27028

In the Matter of The Prudence Company, Inc., Debtor

In the Matter of Amalgamated Properties, Inc., Debtor

In the Matter of a Plan of Reorganization of Amalgamated Properties, Inc., Debtor, in Respect of the Zo-Gale First Mortgage Participation Certificates

Order to Show Cause

Upon the annexed petition of A. Joseph Geist, as trustee, duly verified the 7th day of May, 1940, upon the guaranteed participation certificates, a specimen copy of which is annexed hereto, upon the guaranty agreement executed by The Prudence Company, Inc., annexed hereto, and upon all of the papers and proceedings heretofore had herein, and sufficient reason appearing therefor,

Let the Trustees of The Prudence Company, Inc. and the Prudence Realization Corporation show cause, if any there be, before this Court in Room 224 of the United States Courthouse, Washington and Johnson Streets, Borough of [fol. 4] Brooklyn, City and State of New York, on the 21st day of May, 1940, at 9:30 o'clock in the forenoon of that day, or as soon thereafter as counsel can be heard, why an order should not be made and entered herein declaring that the interest of the Prudence Realization Corporation in and to the outstanding certificates held by the Prudence Realization Corporation in the sum of $816.67 of the Zo-Gale Realty Co. Inc. issue and to the principal amount of the mortgage in the sum of $7,200 of said issue, not represented by outstanding certificates, is subordinate to the certificates issued by Prudence Bonds Corporation and guaranteed by The Prudence Company, Inc. held by certificate holders and that the Trustees of The Prudence Company, Inc., and its successor, Prudence Realization Corporation, are not entitled to any distribution out of the trust estate on account of the shares held by Prudence Realization Corporation until the certificate holders have been paid in full the principal and interest guaranteed them under their certificates, and for such other, further and different relief as to the court may seem just and proper in the premises.

Sufficient Reason Appearing Therefor, let service of a copy of this order and the petition upon which same is based upon Prudence Realization Corporation or upon Irving L. Schanzer, attorney for the Prudence Realization Corporation, on or before the 17th day of May, 1940, be deemed good and sufficient service.

Dated, Brooklyn, New York, May 13th, 1940.

Grover M. Moscowitz, U. S. D. J.

[fol. 5] In United States District Court, Eastern District of New York

[Same Title]

Petition of A. Joseph Geist, Read in Support of Motion

To the Honorable Judges of the United States District Court for the Eastern District of New York:

The petition of A. Joseph Geist respectfully shows to this Court and alleges:

First. That by order duly made and entered in the United States District Court for the Eastern District of New York, on February 1, 1935, the petition of The Prudence Company, Inc. for reorganization under Section 77B of the Bankruptcy Act was approved as duly and properly filed.

Second. That by order duly made and entered in the United States District Court for the Eastern District of New York on March 17, 1936, the petition of Amalgamated Properties, Inc. for reorganization under Section 77B of the Bankruptcy Act was approved as properly filed and was approved as properly filed in the proceedings of The Prudence Company, Inc., Debtor.

Third. That at the time of the filing of the petition of Amalgamated Properties, Inc., The Prudence Company, Inc. was the owner of all of the stock of Amalgamated Properties, Inc., and the trustees of The Prudence Company, Inc., Debtor, appointed by order of the United States District Court for the Eastern District of New York constituted the entire Board of Directors and all of the officers of Amalgamated Properties, Inc.

[fol. 6] Fourth. That on January 28, 1925, The Prudence Company, Inc., the then owner and holder of the first mortgage covering premises #202 Riverside Drive, New York City, and the Zo-Gale Realty Co., Inc., as owner of said premises, entered into a consolidation and extension agreement, whereby the mortgages aggregating the sum of $480,000, affecting said premises, were consolidated and the time of payment of the principal sum of $480,000 was extended to April 1, 1935. Said consolidation and extension agreement was recorded in the office of the Register of New York County on February 2, 1925, in Liber 3526 of Mortgages, Page 456.

Fifth. That thereafter, The Prudence Company, Inc., by an assignment dated January 28, 1925, recorded in the office of the Register of New York County on February 2, 1925, in Liber 3526 of Mortgages, Page 466, assigned the mortgages consolidated and extended pursuant to the agreement hereinbefore described to Prudence Bonds Corporation.

Sixth. That simultaneously therewith, The Prudence Company, Inc. and the Prudence Bonds Corporation en-

tered into an agreement, which provided that the interest of Prudence Bonds Corporation in said consolidated mortgages was $450,000 and that such interest was senior to the interest owned by The Prudence Company, Inc., in the sum of $30,000.

Seventh. That Prudence Bonds Corporation, upon acquiring title to the aforesaid senior interest in said consolidated mortgages, sold undivided interests therein evidenced by guaranteed participation certificates to the public. A specimen copy of the guaranteed participation certificates sold to the public is annexed hereto, marked Exhibit "1", and made a part hereof with the same force and effect as if herein set forth at length.

[fol. 7] Eighth. That The Prudence Company, Inc., pursuant to the terms of a guaranty agreement dated February 5, 1925, guaranteed the payment of principal and interest to the holders of the participation certificates sold by Prudence Bonds Corporation with respect to the consolidated first mortgage in the principal sum of $450,000, which certificates are known as the "Zo-Gale Realty Co. Inc. issue". The mortgage was thereafter reduced by payment to the sum of $390,000. A copy of said guaranty agreement is annexed hereto and marked Exhibit "2" and made a part hereof with the same force and effect as if herein set forth at length.

Ninth. That thereafter, and prior to April 1, 1935, the junior participation interest of $30,000 held by The Prudence Company, Inc. was paid in full.

Tenth. That said guaranty agreement was transferred and delivered to A. Joseph Geist, as trustee for the benefit of the certificate holders, pursuant to the plan of reorganization and the orders of confirmation and consummation.

Eleventh. That by order duly made and entered in the United States District Court for the Eastern District of New York on the 19th day of February, 1938, hereinafter called the "order of confirmation", a plan for the reorganization of the Zo-Gale Certificate Issue, affecting premises #202 Riverside Drive, Borough of Manhattan, City of New York, sponsored by Amalgamated Properties, Inc. was duly approved and confirmed as amended by order of the United States District Court for the Eastern District of New York dated December 10, 1937.

[fol. 8] Twelfth. That the order of confirmation entered on the 19th day of February, 1938, provides in paragraph "7" thereof as follows:

"Some question has arisen with respect to the rights of The Prudence Company, Inc. on account of $816.67 of Certificates held or claimed by that Company and its Trustees, and question has also arisen with respect to the interest in said Mortgage (being the $7,200 principal amount thereof not represented by outstanding Certificates) owned or claimed by The Prudence Company, Inc. and its Trustees and/or by Prudence-Bonds Corporation and its Trustees. Anything in the Amended Plan to the contrary notwithstanding, the Trustee under the Amended Plan shall make no distributions of cash and/or securities on account of the Certificates now held or claimed by The Prudence Company, Inc. and its Trustees, or on account of the part of said Mortgage which is not represented by outstanding Certificates, unless and until it shall have been finally adjudicated by a court of competent jurisdiction that The Prudence Company, Inc. and its Trustees and/or Prudence-Bonds Corporation and its Trustees are entitled to share in the trust estate by reason thereof. Pending final adjudication of such question, said Trustee shall hold in escrow the share of any cash and/or securities distributable under the Amended Plan, to which such Certificates held or claimed by The Prudence Company, Inc. and/or its Trustees would be entitled, if owned and held by someone other than The Prudence Company, Inc. and its Trustees, and the share of any cash and/or securities distributable thereunder to which the part of said Mortgage which is not represented by outstanding Certificates would be entitled if it were represented by outstanding Certificates owned and held by some-[fol. 9] one other than The Prudence Company, Inc. and its Trustees and/or Prudence-Bonds Corporation and its Trustees, and the cash and/or securities so held in escrow by said Trustee shall be distributed by the Trustee without interest, in accordance with the final adjudication of such court: Pending such adjudication, the Certificate so held or claimed by The Prudence Company, Inc., and its Trustees, and the part of said Mortgage which is not represented by outstanding Certificates shall not be subject to purchase out of the sinking fund provided for in said Amended Plan. Without prejudice to the rights, if any, of The Prudence

Company, Inc. and its Trustees, the Trustee under said Amended Plan shall on the closing under said Plan, execute and deliver to Charles H. Kelby and Clifford S. Kelsey, as Trustees of Prudence-Bonds Corporation, a certificate in the name of said Trustees of Prudence-Bonds Corporation, evidencing an interest in the trust estate of $7,200 principal amount and interest, subject, however, to the terms hereof."

Thirteenth. The plan of reorganization, as amended by order dated December 10th, 1937, provides in part thereof as follows:

"The Plan does not contemplate a reorganization of the bond of the Zo-Gale Realty Co., Inc., which is secured by the mortgage, nor a reorganization of the guaranty of The Prudence Company, Inc., and all rights of certificate holders against each of these parties are expressly reserved."

Fourteenth. That on the 9th day of April, 1939, an order, hereinafter called the "order of consummation", was duly made. Said order was entered in the office of the Clerk [fol. 10] of the United States District Court for the Eastern District of New York on the 12th day of April, 1938.

Fifteenth. That your petitioner, as trustee, duly qualified by executing and acknowledging his acceptance of the declaration of trust required to be executed by the order of consummation, and a copy of said trust declaration was thereafter recorded in the office of the Register of the County of New York, and your petitioner has been and now is acting as trustee thereunder.

Sixteenth. On May 20th, 1938, the Prudence Bonds Corporation, Debtor, in reorganization proceedings pending in the United States District Court for the Eastern District of New York, under Section 77B of the Bankruptcy Act, No. 26545, and Charles H. Kelby and Clifford S. Kelsey, as trustees pursuant to the plan of reorganization and the orders of confirmation and consummation assigned, set over, transferred and delivered to your petitioner, as trustee, all right, title and interest of the assignors in and to said bonds, mortgages and other documents then in the possession of the Trustees of Prudence Bonds Corporation.

Seventeenth. That Amalgamated Properties, Inc., pursuant to the plan of reorganization, order of confirmation

and the order of consummation, executed a deed conveying the fee title to the premises to A. Joseph Geist, as trustee, subject to the mortgage in the sum of $390,000, which was extended by agreement between A. Joseph Geist, as trustee, and Amalgamated Properties, Inc.

Eighteenth. That your petitioner herein is the holder of the bond and mortgage and of the fee to the premises and of all the securities delivered pursuant to the plan of reorganization and the orders of confirmation and consum- [fol. 11] mation as trustee, and manages and operates the premises and administers the mortgage, which constitutes the trust estate, for the benefit of the holders of participation certificates, as trustee.

Nineteenth. That thereafter, your petitioner, as trustee, pursuant to the provisions of paragraph "7" of the order of confirmation, and pursuant to the order of consummation, executed and delivered a certificate to the Trustees of The Prudence Company, Inc., certifying to the interest of the said Trustees of an undivided share of $7,200 in the aforesaid mortgage of $390,000 held by your petitioner, as trustee.

Twentieth. That the Trustees of The Prudence Company, Inc. are the registered owners of the following Zo-Gale First Mortgage Participation certificates: #B-2908 in the sum of $800, and #B-2909 in the sum of $16.67.

Twenty-first. That Prudence Bonds Corporation and The Prudence Company, Inc. defaulted in the performance of the terms, covenants and conditions contained in the guaranteed mortgage certificates and in the guaranty agreement, and failed to pay to the holders of the guaranteed mortgage certificates the principal and interest which became due and payable on the guaranteed mortgage participation certificates held by the certificate holders.

Twenty-second. That at all times herein mentioned, Prudence Realization Corporation was and still is a domestic corporation, organized and existing under and by virtue of the laws of the State of New York; the said corporation was organized pursuant to an order of the United States District Court for the Eastern District of New York dated April 21, 1939, in the Matter of The Prudence Company, Inc., Debtor,

[fol. 12] in the Matter of the General Plan of Reorganization proposed by the Reconstruction Finance Corporation; the said corporation succeeded to all of the assets of the trustees of The Prudence Company, Inc., Debtor, including the certificates of the Zo-Gale First Mortgage Participation issue, hereinbefore described.

Twenty-third. That the order of confirmation entered on the 19th day of February, 1938, provides in paragraph "30" thereof as follows:

"The Court retains jurisdiction to hear and determine all questions arising under paragraph 7 of this order with regard to the treatment of Certificates and interests in the trust estate created under the Amended Plan which are held or claimed by The Prudence Company, Inc. and its Trustees and by Prudence-Bonds Corporation and its Trustees, and to take action on any application for an adjudication regarding the final disposition of the cash and/or securities held in escrow pursuant to said paragraph 7 of this order; and the Trustees of The Prudence Company, Inc. and/or the Trustee to be appointed pursuant to the Amended Plan are hereby granted leave to apply at any time at the foot of this order for such adjudication."

Wherefore, petitioner prays for an order declaring that the interest of the Prudence Realization Corporation in and to the outstanding certificate in the sum of $816.67, and to the principal amount of the mortgage in the sum of $7,200 not represented by outstanding certificates is subordinate to the certificates issued by Prudence Bonds Corporation and guaranteed by The Prudence Company, Inc. held by the certificate holders, and that the Trustee of The Prudence Company, Inc. and its successor, Prudence [fol. 13] Realization Corporation, is not entitled to any distribution out of the trust estate on account of the shares held by it until the certificate holders have been paid in full the principal and interest guaranteed them under their certificate, and for such other and further relief as to the Court may seem just and proper in the premises.

Dated, New York, May 7th, 1940.

A. Joseph Geist, Petitioner.

(Verified May 7, 1940.)

EXHIBIT "1" ANNEXED TO PETITION

No. B00000 $

Registered

Prudence First Mortgage Certificate

Guaranteed by

The Prudence Company, Inc.

Prudence-Bonds Corporation, hereinafter called "the Corporation," has received from —— for the purchase of, and hereby assigns to the purchaser, an undivided share equal to that amount, with interest thereon at the rate of —% per annum, in the bond of —— for $—— dated —— 19—, due —— 19—, and in the first mortgage securing the same, covering

[fol. 14] Interest payable —— 1st and —— 1st from —— Date —— 19—.

Specimen, —— — ——, Assistant Secretary; specimen, —— — ——, Vice-President.

This bond and mortgage, together with the guarantee of The Prudence Company, Inc., guaranteeing to holders of this and similar certificates payment of principal and interest, are held by Central Union Trust Company of New York as Depositary and Agent for the holders of such certificates which shall never aggregate more than the amount of principal remaining unpaid on said bond and mortgage upon the following terms and conditions which are agreed to by the holder of this certificate.

1. Central Union Trust Company of New York holds and shall continue to hold said bond and mortgage, said guarantee, and the other instruments and evidences of title relating thereto for the benefit of the purchaser and any other parties interested therein.

2. The Corporation upon the receipt of the interest and principal of said bond and mortgage shall distribute the same pro rata among the parties entitled thereto.

3. The Corporation and/or the Guarantor shall have full power to take any action it may deem necessary or desirable in order to enforce any of the provisions of

said bond and mortgage and to protect the mortgage security.

[fol. 15] 4. The Corporation may for its own corporate account, be the holder or pledgee of similar shares in said bond and mortgage.

5. The Corporation may take up and cancel this certificate at any time on thirty days' notice in writing to the purchaser and payment at one of its offices to be designated in such notice of the amount then owing to the purchaser for the principal and interest.

While the bond secured by the mortgage mentioned in this certificate is payable by its terms on its due date, the policy of The Prudence Company, Inc. entitles it at its option to a period of eighteen months thereafter in which to collect the principal. Regular payment of interest meanwhile is guaranteed.

Central Union Trust Company of New York hereby certifies that the bond and mortgage within referred to, together with the guarantee of payment therein mentioned, the insurance policies and other instruments and evidences of title relating thereto are held by it for the benefit of the parties interested in said bond and mortgage; that the interest of the holder of this certificate in said bond and mortgage is not subordinate to any other shares thereof and is not subject to any prior interest therein.

Central Union Trust Company of New York further certifies that this certificate and all other certificates at any time issued against said bond and mortgage will not exceed the amount of principal owing on said bond and mortgage.

Date —— 19—.

Central Union Trust Company of New York, by ———, Assistant Treasurer, Assistant Secretary.

[fol. 16]

No. B00000

Registered

Prudence First Mortgage Certificate

Guaranteed by

The Prudence Company, Inc.

$ —

Per Cent

Due —— —, ——

Interest payable

The Prudence Company, Inc., hereby certifies and guarantees to the holder of the within certificate that it has guaranteed payment of the principal of the bond and mortgage within mentioned when due or within eighteen months thereafter, and payment of the interest thereon, when due, by guarantee referred to within and now in the possession of the Depositary.

Date —— 19—.

The Prudence Company, Inc., —— — ——, Treasurer; specimen, —— — ——, Secretary.

[fol. 17] EXHIBIT "2" ANNEXED TO PETITION

The Prudence Company, Inc., (hereinafter designated as "this corporation") in consideration of One Dollar and the terms of guarantee named below, guarantees to each and every holder of the certificates of participation issued by Prudence-Bonds Corporation in and to certain bonds and mortgages described in Schedule A who shall give this Corporation notice and proof of ownership (each and every person and corporation to whom under this clause this guarantee runs being hereinafter included in the designation "the insured"):

First: Payment of interest when due according to the terms of each such certificate issued.

Second: Payment of the principal, and of every installment thereof, as soon as collected, but in no event later

than eighteen months after it shall have become due and payment thereof shall have been demanded in writing by the insured, with regular payment meantime of interest at the rate guaranteed:

Terms of Guarantee

By the acceptance of this guarantee this Corporation is made irrevocably the agent of the insured until said certificate of the insured be paid, with the exclusive right, but at its own expense, to sue for and receive the proceeds of any policy of title insurance or fire insurance covering the mortgaged premises; and to collect the principal and interest as it falls due on said bonds and mortgages aforesaid.

This guarantee is subject to the conditions annexed hereto.

[fol. 18] In Witness Whereof, The Prudence Company, Inc. has caused its corporate seal to be hereunto affixed and this instrument to be signed by two of its officers.

Dated the 5th day of February, 1925.

The Prudence Company, Inc., B. Pender, Gertrude I. T. Trundy, Ass't. Secretary.

Schedule A

The bonds covered by this guarantee were made by:

William T. Evans to the Union Dime Savings Bank, dated March 5, 1913, in principal amount $390,000 on which there is now due $362,500.

202 Riverside Drive Corporation to Terrace Court Co. Inc., dated February 19, 1920, in principal amount $95,000 on which there is now due $47,500.

Zo-Gale Realty Co., Inc. to 202 Riverside Drive Corporation, dated August 16, 1920, in principal amount $72,500 on which there is now due $49,000.

Zo-Gale Realty Co., Inc. to The Prudence Company, Inc., dated January 28, 1925 in principal amount $21,000.

All of the above bonds have been duly consolidated and extended pursuant to an agreement between Zo-Gale Realty Co. Inc. and The Prudence Company, Inc., dated January 28, 1925 and they now secure payment of the sum of $480,000 with interest. The mortgages given to secure

[fol. 19] said bonds have been duly recorded and were made between the same parties bearing the same dates as the bonds.

The proper assignments of the above bonds and mortgages into The Prudence Company, Inc. have been duly recorded and an assignment of all the above bonds and mortgages, as consolidated, have been executed by The Prudence Company, Inc. to Prudence-Bonds Corporation, and duly recorded.

This Corporation holds as collateral to said bonds and mortgages a policy of title insurance by Title Guarantee and Trust Company running in favor of Prudence-Bonds Corporation as mortgagee, and policies of fire insurance in the sum of Four Hundred and Fifty Thousand Dollars ($450,000) covering the real property described in said mortgage, which policies are delivered to and deposited with the Central Union Trust Company of New York, as Depositary, for the benefit of the holders of said participating certificates.

The interest of Prudence-Bonds Corporation in this mortgage is to the extent of *$450,000* only. This interest is prior and is equivalent to a first mortgage for *$450,000* and certificates issued are not to exceed *$450,000*.

Conditions

This Corporation is bound:

1—To conduct, without expense to the insured, any action or proceedings which it may deem necessary to enforce the performance of any covenants contained in said bond or mortgage.

2—To continue this guarantee on any extension of said mortgage, unless this Corporation shall elect to collect the amount secured by said mortgage.

[fol. 20] 3—To keep the mortgaged premises insured against fire by policies of fire insurance, having mortgagee clause attached, issued by companies authorized to do business in the State of New York.

4—To require the owner to pay all fire insurance premiums, taxes, assessments and water rates, which are required to be paid by the terms of said mortgage.

5—To consent to the assignment of this guarantee, subject to the terms thereof, to any subsequent owner and

holder of said participating certificates who shall give this Corporation prompt notice and proof of ownership. Unless such notice and proof be given, no subsequent owner or holder shall be entitled to the benefit of this guarantee.

The Insured is bound:

1—To permit this Corporation to collect all interest and the principal secured by said bond and mortgage, and to refrain from collecting any part of the interest or principal secured by said bond and mortgage except through this Corporation.

2—To permit this Corporation to enforce payment of any sums which may be or become due under said bond and mortgage or under any policy of title or fire insurance issued on the premises covered by said mortgage, and to render such reasonable assistance to that end as this Corporation may require, but not to incur any expense in so doing.

All the notices by the insured to this Corporation or by this Corporation to the insured, required or given under this guarantee, shall be in writing and may be sent by mail.

[fol. 21] IN UNITED STATES DISTRICT COURT, EASTERN DISTRICT OF NEW YORK

[Same title]

AFFIDAVIT OF WILLIAM T. COWIN, READ IN OPPOSITION TO MOTION

STATE OF NEW YORK,
County of New York, ss:

William T. Cowin, being duly sworn, deposes and says:

That deponent is President of Prudence Realization Corporation and is the sole remaining Trustee of The Prudence Company, Inc., Debtor. This affidavit is being submitted in opposition to the application of A. Joseph Geist, as Trustee of the Zo-Gale First Mortgage Participation Certificate Issue, for an order determining that the interests of Prudence Realization Corporation in the Zo-Gale Cer-

tificate Issue are subordinate to the certificates held by the general public.

The source of deponent's information are conversations had with employees of Prudence Realization Corporation who were formerly employees of the Trustees and of The Prudence Company, Inc., and examination of the various books of account and records as well as conversations with counsel to Prudence Realization Corporation.

In order to set forth clearly the history of the certificate issue here involved and the facts pertinent to the determination of the parity question, your deponent sets forth in chronological order the sequence of events leading to the instant application.

The Prudence Company, Inc. was an investment corporation organized under Article VII of the New York Banking Law in 1919. It engaged in a guaranty mortgage business and guaranteed single mortgages and 54 certificate [fol. 22] issues in addition to guaranteeing 18 issues of bonds of Prudence-Bonds Corporation, an affiliate. It also issued securities on which it was the primary obligor, including a bond issue generally described as the "1961 Bond Issue" and a certificate issue known as "Prudence B Series". The common stock of Prudence was owned by New York Investors, Inc., the preferred stock being held by the general public. New York Investors, Inc. also owned all of the stock of Prudence-Bonds Corporation.

The certificate issues were created in the following manner: Prudence, having acquired a bond and mortgage with its own funds, assigned such bond and mortgage to Prudence-Bonds Corporation which in turn assigned the said bond and mortgage to a corporate depositary. In some instances a deposit agreement was executed between Prudence-Bonds Corporation and the depositary and in some cases the deposit consisted of a letter of transmittal executed by Prudence-Bonds Corporation and delivered to the depositary together with the instruments of assignment of the bond and mortgage and the guaranty of Prudence. Simultaneously with the assignment of the bond and mortgage by Prudence-Bonds Corporation, Prudence executed an agreement of guaranty and the bond and mortgage and the guaranty were deposited with the depositary. Certificates of participation in the mortgage were issued by Prudence-Bonds Corporation, authenticated by the deposi-

tary and turned over to Prudence who sold them to the general public.

With respect to the Zo-Gale Certificate Issue, Prudence on January 28, 1935, entered into a consolidation and extension agreement with Zo-Gale Realty Co. Inc., as owner of the premises subject to the said certificate issue, whereby mortgages aggregating the sum of $480,000 were consolidated and the time of payment of the principal sum was extended to April 1, 1935. By assignment dated January [fol. 23] 21, 1935, Prudence assigned the mortgages so consolidated and extended to Prudence-Bonds Corporation and entered into an agreement with Prudence-Bonds Corporation which provided that the interest of Prudence-Bonds Corporation in the consolidated mortgages was $450,000 and that such interest was senior to the interest owned by Prudence in the sum of $30,000. Thereafter the junior participation interest of $30,000 held by Prudence was paid in full. No deposit agreement was executed between Prudence-Bonds Corporation and Central Union Trust Company of New York. The sole agreement under which the depositary acted was a letter of transmittal dated February 3, 1925, addressed to Central Union Trust Company by Prudence-Bonds Corporation. A copy of said letter of transmittal is hereto annexed and marked Exhibit "A".

Attached to the petition herein as Exhibit "1" is a specimen certificate for this certificate issue issued by Prudence-Bonds Corporation, and guaranteed by Prudence, and as Exhibit "2", the instrument of guaranty executed by Prudence and deposited with the depositary. The certificate issued by Prudence-Bonds Corporation by its terms does not obligate Prudence-Bonds Corporation to make any payment with respect to the said bond and mortgage nor of the certificates. It constitutes merely an assignment of an undivided interest in the said mortgage to the purchaser.

On May 29, 1932, one Mary Walters, owner of certificate #B-2122 representing a $500 undivided interest in the Zo-Gale Certificate Issue, requested Prudence to reinvest the said sum of $500 in another certificate issue of Prudence-Bonds Corporation guaranteed by Prudence for $500. At the same time certificate #B-2132 for $300 registered in the name of Mary E. Field was reinvested together with other securities for $3,400 in the Fifth Avenue Hotel Certificate Issue. On October 26, 1932, Certificate #B-2891

for $16.67 was issued in the name of The Prudence Com-
[fol. 24] pany, Inc. This certificate was acquired from credit which existed after many cancellations and authentications.

During the early part of 1933 Prudence negotiated with Reconstruction Finance Corporation for a loan of a substantial sum of money and presented to Reconstruction Finance Corporation a list of proposed collateral for such a loan. Included in the said collateral which was offered, was a new certificate, also guaranteed by Prudence, #B-2900 for $800 in the Zo-Gale Certificate Issue which was issued in the name of Reconstruction Finance Corporation in the place and stead of the aforementioned certificates #B-2122 and B-2132 which were then cancelled. On March 1, 1933, certificate #B-2891 was cancelled and certificate #B-2903, also guaranteed by Prudence, for $16.67 was issued in the name of Reconstruction Finance Corporation. Reconstruction Finance Corporation refused to accept this collateral for a further loan to Prudence and on April 4, 1933, the certificates #B-2900 and B-2903 were cancelled and new certificates #B-2908 for $800 and B-2909 for $16.67 were issued in the name of Prudence. At no time prior to the issuance of certificates #B-2908 and B-2909 were the certificates issued in the name of Prudence nor were such certificates at any time cancelled except upon the issuance of a certificate in substitution of such cancelled certificate. It was the intention in each instance upon the acquisition of the aforementioned certificates by Prudence, to hold such certificates as investments and the acquisition by Prudence was not intended at any time to constitute a cancellation or payment under its guaranty.

Moreover, as appears from the books and records of Prudence, such certificates were included in its assets listed on its published financial statements and its own balance sheets.

Certificates of participation were issued by Prudence-Bonds Corporation in the Zo-Gale Certificate Issue for the
[fol. 25] full face amount of the mortgage with the exception of $7,200 which remained as a credit with the depositary which could be called upon by Prudence-Bonds Corporation to authenticate certificates in that amount.

On March 4, 1933, Prudence and other like corporations remained closed for several days pursuant to the proclamation issued by the Governor of the State of New York. At the end of the period of suspension of business neces-

sitated by the Banking Holiday, Prudence on March 16, 1933, resumed business subject to the Regulations issued to it by the Banking Board of the State of New York, and continued to operate under said Regulations at all times from March 3, 1933, to February 1, 1935, the date of the approval for its reorganization under Section 77B. Under the said Regulations of the said Banking Board, in order to avoid preferential expenditures of the funds of Prudence in favor of any creditors, Prudence was prohibited from making any payments out of its general assets to holders of Prudence certificates, either as principal or interest under its guaranty, or as advances for the protection of the property subject to the certificated mortgages. Payments to such holders of certificates and advances for the protection of the certificated mortgages were authorized only out of collections made by Prudence from the mortgagor on the mortgaged property. Under compulsion of such Regulations, Prudence defaulted in the payment of interest due on the Zo-Gale Certificate Issue on April 1, 1933. This was the first default on the guaranty of this issue. Therefore, upon the date of acquisition of the certificates above mentioned in the principal sum of $816.67, Prudence had fulfilled all of its obligations and no default existed with respect to this certificate issue.

In June, 1934, the petition for the reorganization of Prudence-Bonds Corporation under Section 77B of the Bankruptcy Act was approved by Hon. Robert A. Inch, United States District Judge for the Eastern District of New York, [fol. 26] and thereafter on February 1, 1935, the petitions for the reorganization of The Prudence Company, Inc. under Section 77B of the Bankruptcy Act were approved by Hon. Grover M. Moscowitz, United States District Judge for the Eastern District of New York. Upon the approval of the petition for the reorganization of Prudence, an order was entered by its Trustees fixing the procedure for the filing of proofs of claim against Prudence on its guaranty and other obligations. Similar provision was made with respect to claims to be filed against Prudence-Bonds Corporation by the Court in charge of that proceeding.

Thereafter proofs of claim were filed by individual certificate holders in the Zo-Gale Certificate Issue or on their behalf by the depositary in the proceedings for the reorganization of The Prudence Company, Inc., Debtor. In such proofs of claim certificate holders asserted their rights

against Prudence upon the guaranty of principal and interest due on the certificates held by said certificate holders, but in no instance did any certificate holder include in his proof a claim against any certificates or interests which Prudence or its Trustees held in the Zo-Gale Certificate Issue, nor to any priority in distributions on such interests. Attached hereto and marked Exhibit "B" is a copy of a typical proof of claim filed by the Zo-Gale certificate holders against Prudence in the proceedings for its reorganization.

On February 1, 1935, the Prudence Trustees on taking over the assets of The Prudence Company, Inc., Debtor, ascertained that included in the portfolio of assets of the Prudence Estate were bonds of Prudence-Bonds Corporation guaranteed by Prudence in the principal amount of $1,910,300. Claims were filed on such bonds in the proceedings for the reorganization of Prudence-Bonds Corporation and thereafter the question as to whether such bonds shared on a parity with the publicly held bonds was litigated in the United States District Court for the Eastern District of New York. After an adverse determination [fol. 27] against the Prudence Trustees by the Special Master to whom the question had been referred and by the District Court, efforts were made by both sides to compromise this issue and eliminate an appeal. The compromise agreed on by the Trustees of Prudence-Bonds Corporation and the Prudence Trustees and the creditors of both estates were submitted to both Judge Inch and Judge Moscowitz for approval. As part of the said compromise the Prudence Trustees were to withdraw claims filed against Prudence-Bonds Corporation and objections to the plan of reorganization which had been promulgated in that proceeding, and were to receive, in exchange, a cash payment of $150,000 together with all of the rights of Prudence-Bonds Corporation and its Trustees to the uncertificated portion of the various certificate issues, including the $7,200 uncertificated portion of the Zo-Gale Certificate Issue. This latter interest of Prudence-Bonds Corporation and its Trustees was to be transferred to the Prudence Trustees, subject, however, to all claims of general creditors of Prudence-Bonds Corporation and was acquired by the Prudence Trustees in the regular course of business. A copy of the petition and order entered approving the compromise are hereto annexed and marked Exhibit "C". Upon the entry of this order, the compromise was consummated in accordance

with its terms, and the $7,200 uncertificated portion of the Zo-Gale Certificate Issue was transferred to Prudence.

By reason of the default of the mortgagor, the holder of a second mortgage on the property subject to the Zo-Gale Certificate Issue foreclosed its mortgage and by arrangements made with Amalgamated Properties, Inc., a wholly owned subsidiary of Prudence, title was transferred to that corporation on February 1, 1933, by the second mortgagee at the termination of the foreclosure proceeding

On March 16, 1936, the petition for the reorganization of Amalgamated Properties, Inc., a subsidiary of Prudence, was filed and approved by the United States District Court [fol. 88] for the Eastern District of New York. The order entered on the approval of the petition provided for the filing of individual claims by creditors of Amalgamated, including certificate holders, but further provided that claims filed in The Prudence Company, Inc., Debtor reorganization proceedings might be deemed filed in the Amalgamated proceeding and no further necessity existed for the filing of additional claims.

By order to show cause dated May 7, 1937, there was brought on for hearing before this Court in the proceeding for the reorganization of Amalgamated Properties, Inc., Debtor, a motion for the confirmation of the plan of reorganization for the Zo-Gale Certificate Issue which had been proposed by Amalgamated. After hearings held with respect to such plan and amendments and modifications made to it by the Debtor and by the creditors, the plan of reorganization as amended was finally approved by this Court and an order entered in the proceedings for the reorganization of Amalgamated confirming the plan and directing its confirmation. As heretofore set forth, individual proofs of claim filed by certificate holders against Prudence in the proceeding for the reorganization of that corporation, were deemed filed in the Amalgamated proceeding and any further claim filed by certificate holders on their own behalf with respect to the Zo-Gale Certificate Issue were in the same form. In neither proof of claim did any certificate holder assert a right against the certificates held by Prudence or its Trustees in the Zo-Gale Certificate Issue, being content solely to claim in the Prudence proceeding on the personal guaranty of that corporation, and in the Zo-Gale Certificate Issue, for the amount of the certificate holders' participating interest in the mortage.

As part of the plan of reorganization for the Zo-Gale Issue, discussion was had as to the disposition to be made of rights of the Prudence Trustees to participate on a parity with all other certificate holders in the distribution [fol. 29] of the estate represented by the Zo-Gale Certificate Issue. Such questions were left for future determination by provisions of the plan and the order of confirmation as set forth in detail in the petition herein. After the consummation of the plan, the Prudence Trustees received and thereafter assigned to Prudence Realization Corporation certificates representing the interest of the Prudence Trustees in the Zo-Gale Certificate Issue to the extent of issued certificates in the face amount of $816.67 and $7,200 representing the uncertificated portion of the mortgage. Each of these instruments indicated on its face that the question as to the right of distribution of the assets of the Zo-Gale Certificate Issue estate was to be left for future determination.

By order dated May 26, 1939, Hon. Grover M. Moscowitz, United States District Judge for the Eastern District of New York, approved and confirmed the plan of reorganization for Prudence which had been proposed and promulgated by Reconstruction Finance Corporation. A copy of the plan of reorganization and order of confirmation are hereto annexed and marked Exhibit "D". Under the provisions of the said plan of reorganization the rights of all creditors in the distribution of the Prudence Estate were determined. A formula was established for the determination of the final allowance of claims and no provision was made for priority to holders of the Zo-Gale certificates nor of any other certificates held by any other creditor where Prudence or its Trustees held certificates of participation in any certificate issues.

Deponent has been advised by counsel and verily believes that under the circumstances set forth in the petition and in this affidavit, there can be no question that the uncertificated portion of the Zo-Gale mortgage to the extent of $7,200 is held by Prudence Realization Corporation on a parity with the certificates held by the general public. It [fol. 30] must be conceded that in the event that the certificates had been held up to the present time by Prudence-Bonds Corporation, since it was not obligated on either the mortgage or to any person on a guaranty, they would be entitled to participate on a parity with the general

public. So much is clearly established by the law of the State of New York. Moreover, it is also clear under the decisions of the New York State Court that the acquisition of this uncertificated portion of the mortgage by the Prudence Trustees as part of a compromise subject to general claims against Prudence-Bonds Corporation constituted an assignment to the Prudence Trustees of the rights of Prudence-Bonds Corporation and in such capacity the Prudence Trustees acquired the status of their assignors. Under such circumstances, the respondent is entitled to a determination that it shares on a parity with other certificate holders to distributions in the Zo-Gale Issue to the extent, at least, of the $7,200 uncertificated portion of the mortgage.

With respect to the issued certificates in the face amount of $816.67, it is the position of respondent that these certificates were acquired by Prudence for its own corporate account as an investment with the intention that they be so held and not for the purpose of cancellation to extinguish its guaranty obligation. Deponent has been advised by counsel that the decisions in the New York Courts have indicated that where the intention to permit a guarantor to hold certificates on a parity with the general public to which it had assigned other certificates is not clearly set forth in the certificates themselves, the Court will apply an equitable rule authorizing distribution of the proceeds of an estate first to the assignee and next to the assignor. It is submitted that this is a rule of law adopted by the Courts of the State of New York, but not applicable to a bankruptcy proceeding which recognizes no such rule of distribution.

[fol. 31] It is to be noted that on February 1, 1935, the date of the approval of the Prudence petition for reorganization under Section 77B of the Bankruptcy Act, Prudence had already defaulted on its guaranty and any rights to priority in distribution which might at any time exist on behalf of certificate holders in the Zo-Gale Certificate Issue were then established. It is clear that the sole basis, upon which certificate holders may assert the right of priority in distribution from the Zo-Gale Certificate Issue against Prudence or its successor, is the failure of Prudence to fulfill its guaranty. It is the position of Prudence Realization Corporation that when the Zo-Gale certificate holders filed their proofs of claim against Prudence upon such

guaranty, such certificate holders were under an affirmative obligation to elect whether they would consider the participating interest held by Prudence in the Zo-Gale Certificate Issue as further and additional collateral for the performance of the Prudence guaranty to the Zo-Gale Certificate Holders or whether they would rely solely upon their distributive shares of the assets of the Prudence Estate based upon the full amount of their guaranty claim without calling for any priority.

By filing a proof of claim for the full amount of the guaranty obligation without giving credit to the Debtor for the value of the certificates or interest held by Prudence in the Zo-Gale Certificate Issue at that time, the certificate holders made an affirmative election to rely on their claims for the full amount of the guaranty. The remaining $133,000,000 of creditors of Prudence had the right at that time and still continue to have the right to assume that the Zo-Gale certificate holders would only share in the distribution of the assets of the Prudence Estate on their guaranty obligation without receiving in addition any priority in any of the assets constituting that estate. By now asserting a priority right in distributions made by the Zo-Gale Certificate Issue Trustee, certificate holders in that issue are asserting a right not alone to share on a parity with all other creditors in the assets of the Pru-[fol. 32] dence Estate to the extent of the unreduced amount of the guaranty, but in addition to their rights in the primary security (the mortgaged property), these certificate holders assert an affirmative right against that portion of the certificate issue which would ordinarily be distributable to and become part of the Prudence Estate. They are, by the present application, asserting that they hold either additional collateral for their guaranty to the extent of the Prudence interest in the issue, or a right to priority in distribution of the assets of the Prudence Estate as against all other creditors.

Deponent has been advised by counsel and verily believes that under the Bankruptcy Act a creditor who fails to list collateral for the debt in his proof of claim is an unsecured creditor, and is deemed to have waived his rights in the unlisted collateral; nor does it appear that a creditor may, after filing as a general unsecured creditor, assert priority rights. Deponent is advised that no facts exist in the instant case to take this case out of this general rule.

These certificate holders filed claims against Prudence as unsecured creditors. The mortgaged property, owned by a third person, did not constitute part of the Debtor's estate and therefore guaranty creditors were unsecured. However, when the certificate holders assert that in addition to their 381,983.33/390,000ths participating interest in the Zo-Gale mortgage, they may look to Prudence 8016.67/390,000ths interest as collateral for the fulfillment of the Prudence guaranty, they are claiming rights as secured creditors of Prudence, since here the interest of Prudence is an asset of the estate and is properly within the definition of secured creditors. As heretofore noted, upon the election of certificate holders to file claims as unsecured creditors and not to consider the interest held by Prudence in the certificate issue as security for the guaranty, the certificate holders have waived their rights and may not presently assert them to the prejudice of other creditors. [fol. 33] Under the present application, certificate holders ask for preferential treatment which they neither sought nor provided for during the Prudence proceeding. To illustrate the legal situation, we may assume a certificate issue called "X issue", which consists of $200,000 of outstanding certificates of which $190,000 are held by the public and $10,000 by Prudence, where the property earns 2% on the mortgage and can be liquidated for $150,000.

The X certificate holders filed claims *on the Prudence guaranty* for $190,000 against Prudence. The assets of the Prudence Estate including the $10,000 certificates in the issue involved have a face value of $1,000,000, and the total claims including X certificate holders filed against Prudence total $25,000,000.

The X certificate holders now claim:

1. The 2% interest earned by Prudence's $10,000 X certificate shall be paid to them *on their guaranty* and shall not be included in a distributable assets of the estate;

2. Upon liquidation of the property subject to the X Certificate Issue for $150,000, instead of the Prudence Estate receiving its 1/20th interest in the proceeds, or $7,500, that sum shall be turned over to the X certificate holders as part payment *on account of the guaranty obligation* since they are receiving less than full payment out of the proceeds of the property;

3. They shall receive distributions from the Prudence Estate *on the full amount of their guaranty,* in the propor-

tion which their $190,000 claim bears to the total claims of $25,000,000 in assets having a face value of $990,000 ($1,000,000 less $10,000 X certificates).

The result of recognizing these claims is self-evident. By demanding these sums the X certificate holders consider that the $10,000 X certificates held by Prudence are either collateral for their guaranty obligation or that X [fol. 34] certificate holders are entitled to priority in any earnings of the certificates held by Prudence until the guaranty of the X issue is paid in full, without regard to the rights of other guaranty creditors. Not having asserted any such rights against Prudence in its 77B reorganization proceeding where the *guaranty* was reorganized, certificate holders may not now urge such rights after the acceptance and approval of the plan for the guarantor which granted no such extraordinary and additional rights.

The attention of the Court is respectfully called to the fact that the plan for the Zo-Gale Certificate Issue was consummated long prior to the confirmation of the Plan of Reorganization for Prudence. Amended proofs of claim in the Prudence proceeding could have been filed with the approval of the Court up to the time of the confirmation and consummation of the Prudence Plan. No attempts were made to file such amended claims either by such certificate holders or by the Trustee appointed in the certificate issue and your respondent is of the opinion that at the present time any rights which such certificate holders may at any time have had to insist upon priority in distributions in the Zo-Gale Certificate Issue, as against Prudence or its successor, no longer exist.

Wherefore, your respondent prays that the petition herein be in all respects denied and that an order be entered directing the petitioner herein, A. Joseph Geist, as Trustee of the Zo-Gale First Mortgage Participation Certificate Issue, to pay over to respondent all sums presently reserved by such Trustee with respect to the interest held by Prudence Realization Corporation in the Zo-Gale Certificate Issue, and that any distributions made hereafter on said certificate issue be distributed to Prudence Realization Corporation pro rata with other certificate holders.

William T. Cowin.

(Sworn to September 26, 1940.)

13

EXHIBIT "A"

February 3, 1925.
B&M #414

Central Union Trust Company,
80 Broadway,
New York City.

Attention: Mr. F. J. Fuller, Vice-President

Gentlemen:—

We are enclosing herewith for deposit with you the following papers:— 14

1—Bond of William T. Evans to the Union Dime Savings Bank dated March 5, 1913, in principal amount $390,000., on which there is now due $362,500., together with the mortgage given as collateral thereto.

2—Certified copy of assignment of the above bond and mortgage by Union Dime Savings Bank to The Prudence Company, Inc., dated January 29, 1925.

3—Bond of 202 Riverside Drive Corporation to Terrace Court Co., Inc., dated February 19, 1920, in principal amount $95,000., on which there is now due $47,500., together with the mortgage given as collateral thereto.

4—Assignment of the above bond and mortgage by 15
Terrace Court Co., Inc. to Samuel A. Megeath, dated May 7, 1920.

5—Certified copy of assignment of the above bond and mortgage by Samuel A. Megeath to The Prudence Company, Inc. dated January 29, 1925.

16 *Exhibit "A".*

6—Bond of Zo-Gale Realty Co., Inc. to 202 Riverside Drive Corporation dated August 16, 1920 in principal amount $72,500. on which there is now due $49,000., together with the mortgage given as collateral to said bond.

7—Assignment of the above bond and mortgage by 202 Riverside Drive Corporation to Kentucky Holding Co., Inc., et al, dated December 21, 1920.

8—Certified copy of the assignment by Kentucky Holding Co., Inc., et al to The Prudence Company, Inc. dated January 27, 1925.

17 9—Bond of Zo-Gale Realty Co., Inc. to The Prudence Company, Inc. dated January 28, 1925, in principal amount $21,000. together with the certified copy of the mortgage given as collateral to said bond.

10—Certified copy of agreement between Zo-Gale Realty Co. Inc. and The Prudence Company, Inc., dated January 28, 1925 consolidating all of the above bonds and mortgages into one lien of $480,000. and extending the terms thereof.

11—Certified copy of an ownership agreement executed between The Prudence Company, Inc. as party of the first part and Prudence-Bonds Corporation as party of the second part, dated January 28, 1925 wherein Prudence-Bonds Corporation is given a prior interest of $450,000 in the lien of $480,000.

18

12—Certified copy of assignment of all the above bonds and mortgages by The Prudence Company, Inc. to Prudence-Bonds Corporation, dated January 28, 1925.

13—Guarantee of The Prudence Company, Inc. dated February 3, 1925.

Exhibit "A".

14—Policy of Title Guarantee & Trust Company No. 925343 insuring the lien of said mortgaged premises.

15—Fire insurance binder covering the said mortgaged premises.

16—Appraisal of Realty Associates dated January 30, 1925 showing the value of the mortgaged premises to be 50% greater than the amount of certificates outstanding at any one time.

Will you kindly hold possession of these enclosures and from time to time certify Prudence First Mortgage Certificates delivered to you for certification against the said securities. These certificates will be in similar form to those heretofore used by us in these transactions.

We understand that your fees in this matter will be upon the same scale as heretofore used in our matters.

Will you kindly acknowledge receipt of these papers by signing and returning to us the copy of this letter enclosed herewith for that purpose?

Yours very truly,

PRUDENCE-BONDS CORPORATION
By:
F. T. Pender (signed)
Secretary.

FTP:DL

Feb. 6-1925

The above instruments duly received.

CENTRAL UNION TRUST COMPANY OF N. Y.
C. F. Carey (Signed)
Corporate Trust Department.

22

EXHIBIT "B"

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK.

IN THE MATTER OF THE PRUDENCE COMPANY, INC., Debtor.	In Consolidated Proceedings for Reorganization under Section 77B of the Bankruptcy Act. Nos. 27496 and 27028.

STATE OF PENNSYLVANIA }
23 COUNTY OF DELAWARE } ss.:

On the 16th day of October 1935, came ALEXANDER H. BASS of R. F. D. No. 3 of Media, in the State of Pennsylvania and made oath and says:

1. That this claim is made in deponent's own behalf.

3. That the claimant was on February 1, 1935, the date of the approval of the petitions for the reorganization of the Debtor herein, and still is, the lawful owner and holder of Prudence-Bonds Corporation mortgage participation certificate(s), and, if the same be not registered, of the coupons appurtenant thereto, which mortgage participation certificate(s) are described as follows:

24

Serial Number	*Interest Rate*	*Principal Amount*	*Name of Issue*
Ctfs B.2934/7	5½%	$40,000.00	ZO-GALE REALTY CO. INC.
B.2922/9	.....	$.....	.....
	Total	$40,000.00	

the bond(s) and mortgage(s) referred to in the said mortgage participation certificate(s) having been deposited with the Depositary or Depositaries therein mentioned; that in form, the Prudence Company, Inc. guaranteed payment of principal and interest as provided in an instrument executed by The Prudence Company, Inc. and deposited with the said Depositary or Depositaries; that the foregoing constitutes a statement of claimant's claim herein, and that the consideration therefor was the payment of moneys for the purchase of said mortgage participation certificate(s) by the claimant or claimant's predecessor in title.

4. Based upon the foregoing, a sum equal to the unpaid principal of said mortgage participation certificate(s) and the interest thereon to February 1, 1935, now unpaid, is justly owing from the Debtor to the claimant; that there are no set-offs or counter-claims to the same, but the claim is subject to reduction by any payments received on account of principal and/or interest on said mortgage participation certificate(s) subsequent to the filing of this proof of claim; that upon said indebtedness no note or other evidence of indebtedness, except as aforesaid, has been received, and no judgment has been rendered thereon, and neither said claimant, nor to this deponent's knowledge and belief, has any person, by order of said claimant and to his use, had or received any manner of security for said indebtedness, except to the extent that the bond(s) and mortgage(s) deposited with the said Depositary or Depositaries as aforesaid, may be security for the said debt.

ALEXANDER H. BASS (L. S.)
(Signature)

28 *Exhibit "B".*

Address to which all notices shall be sent:

R. F. D. #3 Media, Pa.

Subscribed and sworn to before me
this 16 day of October, 1935.

HELEN V. HARBOLD
Notary Public
My Commission Expires March 20, 1939

29

30

EXHIBIT "C"

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

IN THE MATTER
OF
THE PRUDENCE COMPANY, INC.,
Debtor.

In Consolidated Proceedings for Reorganization under Section 77B of the Bankruptcy Act.

Nos. 27496 and 27028

In the Matter of the Application of the Trustees of the Debtor for an order approving a settlement and compromise of the claims of the estate of The Prudence Company, Inc. against Prudence-Bonds Corporation and its estate, and authorizing and directing the settlement and compromise of the same.

Upon the annexed petition of Stephen Callaghan, John M. McGrath and William T. Cowin, Trustees of the Debtor herein, duly verified the 15th day of December, 1937, with the exhibits thereto attached and referred to therein and upon all the papers filed and the proceedings heretofore had herein,

LET, the Debtor herein, all parties and intervenors herein, all creditors and stockholders of The Prudence Company, Inc. and all other parties interested in the above entitled proceedings, or their respective attorneys or solicitors in the above entitled proceedings, show cause before me at a Stated Term of this Court to be held in Room 224 of the United States Court House, at the corner of Washington and Johnson Streets in the Borough of Brooklyn, City and State of New York on the 30th day of

December, 1937 at 2:00 o'clock in the afternoon of said day, or as soon thereafter as counsel can be heard, why an order should not be made and entered herein (a) approving an agreement of settlement embodied in Exhibits "A" and "B" annexed to the said petition; (b) authorizing and empowering the said petitioners as Trustees of the Debtor herein to carry out the said settlement agreement; and (c) authorizing and empowering the said petitioners as Trustees of the Debtor herein to do all acts necessary and to execute all papers, documents or other instruments in writing proper and necessary to carry out the said settlement agreement and (d) for such other and further relief as may be proper
35 in the premises.

SUFFICIENT CAUSE APPEARING THEREFOR,

LET, service of this order and the petition upon which it is granted, by service of copies thereof on or before December 18th, 1937 upon the Debtor herein and upon all intervenors in this proceeding or their respective attorneys appearing herein and the Clerk of this Court, who shall forthwith give proper notice thereof to the Secretary of the Treasury of the United States, and by publication of a notice in substantially the form hereto annexed, marked "Exhibit A" once in the Brooklyn Daily Eagle and New York Evening Post, two (2) newspapers in general circulation in this district, on or before December 20, 1937, be deemed sufficient service upon and notice of this appli-
36 cation to the Debtor, to all parties and intervenors herein, to the Secretary of the Treasury of the United States, to all creditors and stockholders of The Prudence Company, Inc. and to all parties and intervenors otherwise interested in the above entitled proceedings.

Dated: Brooklyn, New York
December 15, 1937.

GROVER M. MOSCOWITZ
U. S. D. J.

EXHIBIT A

THE PRUDENCE COMPANY, INC., DEBTOR IN REORGANIZATION.

Notice to creditors, stockholders and all parties interested in the reorganization proceedings.

PLEASE TAKE NOTICE, that upon the petition of the undersigned and the order to show cause dated December , 1937 made thereon by the United States District Court for the Eastern District of New York in the proceedings pending in said Court entitled "In the Matter of The Prudence Company, Inc., Debtor, in proceedings for reorganization under Section 77B of the Bankruptcy Act, Numbers 27496 and 27028", a hearing will be held at said Court in Room 224 in the Federal Building, Washington and Johnson Streets, Brooklyn, New York, on , 1937 at 2:00 o'clock in the afternoon of said day, or as soon thereafter as counsel can be heard, why an order should not be made and entered in said proceedings authorizing and approving a settlement and compromise of certain claims of The Prudence Company, Inc., and of the undersigned as its Trustees, against Prudence-Bonds Corporation and its Estate including, among other things, a settlement of the litigation respecting the status of Prudence-Bonds owned by the undersigned and further including a settlement of other claims made on behalf of the Estate of The Prudence Company, Inc. in the proceedings for reorganization of Prudence-Bonds Corporation and further including authority to the undersigned to execute consents to the plans of reorganization for the eighteen series of Prudence Bonds and to the amended general plan of reorganization and to authorize the undersigned to take all necessary steps and to execute all necessary documents, to carry out the aforesaid settlement agreement and to effectuate its substance and intent.

Exhibit "C".

The aforesaid hearing may be adjourned from time to time without further notice other than the announcement of the adjourned date at the hearing.

The petition upon which the aforesaid order to show cause was made, together with the agreement of settlement annexed to said petition, is on file in the office of the Clerk of said Court and copies thereof may be inspected by parties interested at the office of the undersigned.

Published by order of the Court.

Dated: December , 1937.

STEPHEN CALLAGHAN, JOHN M. McGRATH and WILLIAM T. COWIN, Trustees of The Prudence Company, Inc.,
331 Madison Avenue,
New York, N. Y.

Exhibit "C".

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK.

IN THE MATTER

OF

THE PRUDENCE COMPANY, INC.,

Debtor.

In Consolidated Proceedings for Reorganization under Section 77B of the Bankruptcy Act.

Nos. 27496 and 27028.

In the Matter of the Application of the Trustees of the Debtor for an order approving a settlement and compromise of the claims of the estate of The Prudence Company, Inc. against Prudence-Bonds Corporation and its estate, and authorizing and directing the settlement and compromise of the same:

PETITION

To the Honorable the Judges of the United States District Court for the Eastern District of New York:

The petition of Stephen Callaghan, John M. McGrath and William T. Cowin, as Trustees of the above-named Debtor, respectfully shows:

1. Your petitioners were appointed temporary trustees of The Prudence Company, Inc., Debtor, by an order made in the above entitled proceedings on February 1, 1935, and the appointment of your petitioners as such Trustees was made permanent by an order of this Court made on March 8, 1935. Your petitioners have duly qualified and are now

acting as such Trustees of The Prudence Company, Inc., Debtor.

2. Your petitioners are informed and verily believe that prior to said February 1, 1935, Prudence-Bonds Corporation had issued and was obligor upon eighteen (18) separate issues of first mortgage collateral trust bonds, payable to the bearer or registered holder thereof, aggregating in principal amount approximately Fifty-six Million Dollars ($56,000,000); that each such bond issue is secured by a separate trust indenture made between Prudence-Bonds Corporation and a Bank or Trust company, under which
47 first mortgages and mortgage bonds and other securities were pledged by Prudence-Bonds Corporation, which securities constitute the collateral underlying said bond issues, and that the present names of the Trustees or successor Trustees of said eighteen (18) issues of bonds are as follows:

Series A	Guaranty Trust Company of New York
Series AA	City Bank Farmers Trust Company
Third Series	City Bank Farmers Trust Company
Fourth Series	City Bank Farmers Trust Company
48 Fifth Series	Bank of the Manhattan Company
Sixth Series	Central Hanover Bank & Trust Company
Seventh Series	City Bank Farmers Trust Company
Eighth Series	Brooklyn Trust Company
Ninth Series	Bank of the Manhattan Company

Tenth Series	State Street Trust Company
Eleventh Series	Chicago Title and Trust Company
Twelfth Series	Manufacturers Trust Company
Thirteenth Series	Manufacturers Trust Company
Fourteenth Series	The Chase National Bank of the City of New York
Fifteenth Series	Chemical Bank and Trust Company
Sixteenth Series	The Marine Midland Trust Company of New York
Seventeenth Series	City Bank Farmers Trust Company
Eighteenth Series	Central Hanover Bank & Trust Company

3. Your petitioners are informed and verily believe that all of said Banks or Trust Companies have a principal office or place of business in the City and State of New York, with the exception of State Street Trust Company, which has its principal place of business in the City of Boston, State of Massachusetts, and Chicago Title and Trust Company, which has its principal place of business in the City of Chicago, State of Illinois.

4. Your petitioners are informed and verily believe that prior to February 1, 1935, The Prudence Company, Inc. had guaranteed the said bonds both as to principal and interest.

5. Your petitioners are informed and verily believe that prior to February 1, 1935, said Prudence Bonds Corporation had issued and The Prudence Company, Inc. had

guaranteed both as to principal and interest fifty-four (54) mortgage certificate issues aggregating in principal amount approximately fifty-three million ($53,000,000) dollars; that each of such certificate issues represents participating certificates issued by Prudence-Bonds Corporation in a single bond and mortgage or a consolidated bond and mortgage on real estate; that Prudence-Bonds Corporation was not obligated on the said certificates.

6. Your petitioners are informed and verily believe that there are approximately thirty thousand holders of the outstanding bonds of the said eighteen (18) issues of bonds and that there are approximately twenty-three thousand
53 (23,000) holders of the outstanding certificates of the said fifty-four (54) certificate issues.

7. Your petitioners are informed and verily believe that on June 29, 1934, Prudence-Bonds Corporation filed its petition in this Court for reorganization under Section 77B of the Bankruptcy Act, and on the same day this Court entered its order approving said petition as properly filed under said Section 77B, and appointed Charles H. Kelby and Clifford S. Kelsey, as temporary trustees of Prudence-Bonds Corporation under that section, and by order entered on July 31, 1934, the appointment of said temporary trustees was made permanent by this court, and the said Charles H. Kelby and Clifford S. Kelsey duly
54 qualified and are now acting in that capacity.

8. Your petitioners are informed and verily believe that on February 1, 1935, the date of the approval of the petition for reorganization herein, and the appointment of your petitioners as Trustees of the Debtor herein, there were among the assets of The Prudence Company, Inc. and there came into the possession of your petitioners as Trus-

tees thereof, bonds of the said eighteen (18) series in the aggregate face amount of One Million Nine Hundred Ten Thousand Three Hundred ($1,910,300) Dollars.

9. Your petitioners are informed and verily believe that prior to the appointment of your petitioners as Trustees of the Debtor herein, Milton L. Masson, Special Deputy Superintendent of Banks, had filed or caused to be filed proofs of claim on behalf of the estate of The Prud[illegible]e Company, Inc. in the proceedings for reorganization of Prudence-Bonds Corporation. Annexed hereto is a letter dated December 9, 1937, and marked Exhibit "A", which in paragraph "3" thereof contains a general description of all such claims, and which claims are incorporated herein at this point as if set forth in full.

10. After the appointment of your petitioners as Trustees aforesaid, certain of the corporate trustees of the said eighteen (18) bond issues described in paragraph "2" hereof made distributions out of principal and/or income of the collateral in their possession as Trustee to owners and holders of bonds of the respective eighteen series, but wholly refused to pay over to your petitioners their pro rata share of such distributions with respect to the bonds of such issues owned and held by your petitioners as trustees aforesaid, and comprised in the bonds aggregating One Million Nine Hundred Ten Three Hundred ($1,910,300) Dollars, described in paragraph "8" hereof. Thereafter and pursuant to leave granted by an order of this court made on January 20, 1936, your petitioners moved in the proceedings for the reorganization of Prudence-Bonds Corporation pending in this court, for an order directing the said corporate trustees to make the said distribution to your petitioners on account of said bonds owned and held by your petitioners, as aforesaid. The said corporate trustees, by their answers, raised the issue as to whether

or not the bonds owned and held by your petitioners in the said eighteen (18) bond issues were entitled to parity of treatment with bonds held by the general public, the said corporate trustees contending that the said bonds were subordinate in all respects to other outstanding bonds of the said series.

11. Your petitioners are informed and verily believe that thereafter, the matter was referred by order of Hon. Robert A. Inch to James G. Moore, as Special Master, and there ensued extended hearings and lengthy testimony with respect to the said bonds. The said Special Master filed two reports, one dated December 8, 1936, dealing with bonds of Series A, AA, Fourth, Sixth, and Eighteenth Series, and another dated April 28, 1937, dealing with the remainder of the thirteen series of Prudence-Bonds owned by your petitioners. The reports of the Special Master were in substance adverse to the claim of your petitioners for parity and equality of treatment and recommended that the said bonds be treated as subordinate. On July 21, 1937, in said proceedings for the reorganization of Prudence-Bonds Corporation, Honorable Robert A. Inch made an order approving the said Special Master's reports and adjudicating and holding that the Prudence Bonds of said eighteen (18) series owned and held by your petitioners are subordinate both as to principal and interest to all other bonds of the said eighteen issues owned by the general public.

12. Your petitioners will offer to the court on the hearing of this application a copy of a record of all of the proceedings relating to the litigation of this question of the status of said One Million, Nine Hundred Ten Thousand Three Hundred ($1,910,300) Dollars of bonds. An appeal has been taken by your petitioners from the said order of July 21, 1937 and from the said determination

of the status of the bonds owned and held by your petitioners, but said appeal has not yet been argued or heard in the Circuit Court of Appeals for the Second Circuit to which the said appeal was taken.

13. Your petitioners are informed and verily believe that plans of reorganization for each of the eighteen bond issues of Prudence-Bonds Corporation were proposed by said Prudence-Bonds Corporation and by orders made in said Prudence-Bonds Corporation reorganization proceedings, this Court found that such plans had been duly proposed in accordance with Section 77B of the Bankruptcy Act. Thereafter, all said plans and all objections, modifications or amendments thereto were referred to James G. 62
Moore, Esq., as Special Master for consideration and report. Thereafter, hearings were held before said Special Master and the said Special Master filed reports approving, with certain modifications and amendments, separate plans of reorganization for all of the said eighteen series of bond issues. Said plans of reorganization, the reports thereon and the relevant orders of this Court with respect thereto are on file in the office of the Clerk of this Court, and are incorporated by reference at this point as if set forth in full. All of such plans in substance provide with respect to bonds of the eighteen series held by your petitioners that they shall be given the treatment to which they shall be legally entitled. Copies of said plans of reorganization will be offered to the Court at the hearing on this 63
application.

14. Your petitioners are informed and verily believe that Prudence-Bonds Corporation also proposed herein a general plan for the reorganization of its general assets and liabilities and by an order of this Court duly entered in the proceedings for the reorganization of Prudence-Bonds Corporation, the Court found that such plan had been prop-

erly proposed in accordance with section 77B of the Bankruptcy Act, and such plan and all objections or amendments thereto were also referred to Honorable James G. Moore, Esq., as Special Master for consideration and report with his opinion thereon.

15. Your petitioners are informed and verily believe that on or about March 11, 1937, said Special Master filed his report approving with certain modifications and amendments the said general plan of reorganization. That the Special Master in his report found that Prudence-Bonds Corporation is insolvent, and that in respect of each of the eighteen (18) separate issues of outstanding bonds of
65 Prudence-Bonds Corporation the present fair value of the collateral pledged to secure such issue is less than the principal amount of the outstanding bonds of such issue and accrued interest thereon, and that Prudence-Bonds Corporation, its stockholders and general creditors have no equity in said pledged collateral in any series of said bonds. Upon information and belief, such general plan of reorganization, as amended, contemplates the organization of a new corporation, which is to be owned and controlled exclusively by the bondholders of the eighteen series or creditors. By an order made in said proceedings for the reorganization of Prudence-Bonds Corporation on April 27, 1937, this Court found that Prudence-Bonds Corporation is insolvent, and tentatively approved the said amended general plan of
66 reorganization, subject to final confirmation in accordance with section 77B of the Bankruptcy Act. All of the foregoing reports and orders are incorporated by reference at this point as if set forth in full.

16. Your petitioners are informed and verily believe that the necessary acceptances from bondholders of each of the eighteen (18) series have been received by the Trustees of Prudence-Bonds Corporation and that applications

were made or are being made by said Trustees for confirmation of the said plans of reorganization for the said eighteen (18) series of bond issues, and for confirmation of the amended general plan of reorganization.

17. Your petitioners are informed and verily believe that the claims heretofore filed on behalf of The Prudence Company, Inc., and referred to in paragraph "10" hereof includes a claim by The Prudence Company, Inc. for advances aggregating Nine Hundred Eighty-seven Thousand Seven Hundred and Forty-three and 61/100 ($987,743.61) Dollars, which advances were made by The Prudence Company, Inc. for the protection of property or collateral securing the said eighteen (18) issues of Prudence-Bonds, and for the payment of interest on such bonds. In addition said claims include the claim of The Prudence Company, Inc. to the ownership of "unissued certificates", i.e. the difference between the face amount of mortgages certificated in the said fifty-four (54) mortgage participation certificate issues, and the face amount of certificates actually issued and to "unissued bonds," i.e. bonds representing the difference between the face amount of collateral deposited in any one of the eighteen issues and the face amount of bonds actually outstanding. 68

18. Your petitioners are informed and verily believe that when motions were made to confirm the said plans of reorganization for the said eighteen (18) series of Prudence-Bonds, and said amended general plan of reorganization, your petitioners caused answers, objections and exceptions to be filed in which your petitioners contended inter alia that the applications for confirmation of the plans were premature in view of the fact that there was pending the so-called "parity appeal" described in paragraph "13" hereof. Your petitioners urged that even if the said order of July 21, 1937, subordinating the bonds 69

of the eighteen (18) series owned by your petitioners, should be confirmed, that your petitioners would then as such subordinate bondholders constitute a separate class of creditors for whom no provision was made in the said plans of reorganization and whose consents were required.

19. Your petitioners further objected to the provisions of the amended general plan of reorganization upon the ground that any surplus that might arise in any bond issue should be applied first to the repayment of advances made by The Prudence Company, Inc., the nature of which is described in paragraph "16" hereof, before being applied
71 generally to other bond issues. The said motions to confirm the said plans of reorganization and the said amended plan of reorganization are still pending undetermined and no decision has been made on the answer, objections or exceptions of your petitioners.

20. Pending the said parity appeal and pending the said motions for confirmation, your petitioners and their solicitors entered into negotiations with Charles H. Kelby and Clifford S. Kelsey, and their solicitor, looking toward a settlement of these numerous claims and of the parity issue. The result of these negotiations is embodied in a letter of offer dated December 9, 1937, from your petitioners, a copy of which is annexed hereto and marked Exhibit "A", and acceptance thereof dated December 13, 1937, signed by
72 Charles H. Kelby and Clifford S. Kelsey, Trustees of Prudence-Bonds Corporation, accepting the said offer. A copy of the said letter of acceptance is annexed hereto and marked Exhibit "B".

21. Your petitioners believe that the said settlement is a desirable one and beneficial to the estate of The Prudence Company, Inc. and to its creditors (including bondholders of the eighteen series of Prudence-Bonds) and to all other persons interested in the estate of the Debtor.

22. Your petitioners believe that the effect of the settlement would be to give to your petitioners, first, the "unissued certificates" and any other interest of Prudence-Bonds Corporation in the said fifty-four (54) mortgage participation certificate issues, as between Prudence and Prudence-Bonds Corporation. A further effect will be to give to the estate of The Prudence Company, Inc. a sum approximating One Hundred and Fifty Thousand ($150,000) Dollars in cash. It will further make possible a speedier consummation of the plans of reorganization for the eighteen series of bond issues, by disposing of the necessity for taking and perfecting an appeal to the Circuit Court of Appeals on the "parity" issue.

23. Your petitioners believe that the claim respecting the Nine Hundred Eighty-seven Thousand Seven Hundred Forty-three and 61/100 ($987,743.61) Dollars, even though the same be a valid claim, has no possibility of immediate reduction and realization in actual cash. Under such circumstances it cannot be considered a substantial obstacle to a settlement which contemplates immediate receipt by your petitioners of approximately One Hundred Fifty Thousand (150,000) Dollars in cash. Your petitioners show, with respect to the surrender of the claim to unissued bonds (said claim being for $153,289.81, the face amount of such bonds), that apart from any consideration of the legal validity of the said claim (particularly in view of the fact that both Prudence-Bonds Corporation and The Prudence Company, Inc. are in default with respect to the said bond issues) such bonds even if received by your petitioners would occupy the same subordinate position in the event of the affirmance by the Circuit Court of Appeals as bonds already owned by your petitioners in the eighteen (18) series. Under such circumstances your petitioners believe that a settlement which contemplates the surrender of these claims in exchange for a present cash consideration will be advantageous to this Estate.

24. Your petitioners are desirous of enabling the approximately thirty thousand (30,000) holders of bonds of the eighteen (18) series, of whom more than sixty-six and two thirds (66-⅔%) per cent have expressed their approval of the Prudence-Bonds plans of reorganization, to consummate their reorganizations. By agreeing to this settlement your petitioners facilitate such consummation. Your petitioners believe that it will be to the best interests of the creditors of the Estate of the Debor herein to assist in the early consummation of the plans of reorganization of Prudence-Bonds Corporation. Your petitioners are also desirous of saving the estate of The Prudence Company,
77 Inc. the expense attendant upon the appeal on the parity issue, in which the decision of both the lower court and of the Special Master has been adverse to the claim of your petitioners.

25. Your petitioners do not believe that the withdrawal of the proofs of claim described in paragraphs "3" of Exhibit "A" and numbered therein II and VI, will result in any loss to this Estate. The proof of claim numbered II is a proof of claim having to do with Prudence-Bonds and/or mortgage participation certificates deposited as collateral by The Prudence Company, Inc. to secure The Prudence Company's 5-½% collateral trust bonds due May 1, 1961, and your petitioners are informed that Central Hanover Bank and Trust Company as corporate trustee
78 therefor has filed proofs of claim thereon. With respect to proof of claim numbered VI, your petitioners show that Prudence-Bonds Corporation was not obligor on Prudence certificates nor liable thereon, and that, therefore the surrender of this claim is not a surrender of a claim based upon any liability.

26. Your petitioners ask for an order to show cause in order that your petitioners may be instructed as to the

79

method of service hereof, and in order that an expeditious hearing thereon may be had.

WHEREFORE, your petitioners respectfully pray that an order be made directing the Debtor herein, all intervenors herein, all creditors and stockholders of The Prudence Company, Inc., and all other parties interested herein, to show cause why an order should not be made approving the settlement agreement embodied in Exhibits "A" and "B" annexed hereto; authorizing and empowering your petitioners to carry out the said settlement agreement; and authorizing and empowering your petitioners to do all acts and to execute all papers, documents or other instruments in writing proper and necessary to carry out the said settlement agreement.

80

Dated, New York, New York,
December 15, 1937.

STEPHEN CALLAGHAN
JOHN M. MCGRATH
WILLIAM T. COWIN
Petitioners.

81

82 *Exhibit "C".*

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

STEPHEN CALLAGHAN, being duly sworn, deposes and says that he is one of the petitioners named in the within petition; that he has read the said petition and knows the contents thereof; that the same is true of his own knowledge, except as to the matters therein stated to be alleged on information and belief, and that as to those matters he believes same to be true.

STEPHEN CALLAGHAN

Sworn to before me this
15th day of December, 1937.

83 RICHARD J. HORRIGAN,
Notary Public
Kings Co. Clks. No. 457 Reg. No. 9169
N. Y. Co. Clerks No. 495, Reg. No. 9-H-349
Commission expires March 30, 1939

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

JOHN M. MCGRATH, being duly sworn, deposes and says that he is one of the petitioners named in the within petition; that he has read the said petition and knows the contents thereof; that the same is true of his own knowledge, except as to the matters therein stated to be alleged on information and belief, and that as to those matters he
84 believes same to be true.

JOHN M. MCGRATH

Sworn to before me this
15th day of December, 1937.

RICHARD J. HORRIGAN,
Notary Public
Kings Co. Clks. No. 457 Reg. No. 9169
N. Y. Co. Clerks No. 495, Reg. No. 9-H-349
Commission expires March 30, 1939

Exhibit "C",

85

STATE OF NEW YORK }
COUNTY OF NEW YORK } ss.:

WILLIAM T. COWIN, being duly sworn, deposes and says that he is one of the petitioners named in the within petition; that he has read the said petition and knows the contents thereof; that the same is true of his own knowledge, except as to the matters therein stated to be alleged on information and belief, and that as to those matters he believes same to be true.

WILLIAM T. COWIN

Sworn to before me this
15th day of December, 1937.

86

RICHARD J. HORRIGAN,
Notary Public
Kings Co. Clks. No. 457 Reg. No. 9169
N. Y. Co. Clerks No. 495, Reg. No. 9-H-349
Commission expires March 30, 1939

EXHIBIT A

December 9, 1937.

Charles H. Kelby and Clifford S. Kelsey, Esqs.
Trustees of Prudence-Bonds Corporation
331 Madison Avenue
New York, N.Y.

87

Dear Sirs:

Subject to the approval of the court having jurisdiction in the proceedings for the reorganization of Prudence-Bonds Corporation and subject to the approval of the court having jurisdiction over the proceedings for the reorganization of The Prudence Company, Inc., we propose the following:

(1) We will accept subordination of the Prudence-Bonds of the eighteen series owned and held by us as Trustees

88 *Exhibit "C".*

of The Prudence Company, Inc., in the aggregate principal face amount of $1,910,300.00 as subordination is defined in paragraph 11 of the several plans of reorganization for the eighteen series of bond issues and also as provided for and defined in the order of Hon. Robert A. Inch made on July 21, 1937. We will submit our bonds for stamping with an appropriate legend indicating such subordination.

(2) We will withdraw and discontinue the pending appeal from the order of Hon. Robert A. Inch made in the proceedings for the reorganization of Prudence-Bonds Corporation on July 21, 1937 and commonly referred to as "the
89 parity appeal".

(3) We will withdraw and consent to the expunging of all of the following proofs of claim heretofore filed by or on behalf of The Prudence Company, Inc. in the proceedings for the reorganization of Prudence-Bonds Corporation, and will release any and all of our rights, liens and interests with respect thereto against said Prudence-Bonds Corporation and its estate including its pledged collateral not specifically reserved herein, which claims are generally described as follows, to wit:

General Nature of Claim	*Amount*
1. Proof of claim verified November 30, 1934, by Milton L. Masson, Special
90 Deputy Superintendent of Banks, being in substance a claim for (a) Guarantees of The Prudence Company, Inc. of Prudence bonds and Prudence certificates, and (b) The Constructive Trust Resulting Trust and all other rights, claims and equities in favor of The Prudence Company, Inc. against Prudence-Bonds Corporation.	No amount stated

Exhibit "C".

	General Nature of Claim	*Amount*
II.	Proof of claim verified November 30, 1934, by Milton L. Masson, Special Deputy Superintendent of Banks, being in substance a claim for 1961 Bonds and 1961 Trust Fund; proof of claim being filed (a) on behalf of The Prudence Company, Inc. in respect of the 1961 bonds owned by it and the surplus of (or residual right in) the 1961 Trust Fund, over and above the amount thereof required to liquidate all the 1961 bonds (whether owned by The Prudence Company, Inc. or others), and (b) on behalf of all holders of 1961 bonds other than The Prudence Company, Inc., in respect of the 1961 bonds held by them and the lien thereof on the 1961 Trust Fund.	No amount stated
III.	Proof of claim verified November 30, 1934, by Milton L. Masson, Special Deputy Superintendent of Banks, being in substance a claim for Prudence Bonds and Trust Funds; proof of claim being filed, (a) on behalf of The Prudence Company, Inc., in respect of Prudence Bonds owned by it and surplus of (or residual right in) the respective Trust Funds over and above the amounts thereof required to liquidate all the Prudence bonds (whether owned by The Prudence Company, Inc. or others) of the respective series of Prudence bonds, and (b) on behalf of all holders of Prudence bonds other than	No amount stated

94 *Exhibit "C".*

	General Nature of Claim	*Amount*
	The Prudence Company, Inc. in respect of the Prudence bonds and the lien thereof upon the respective Trust Funds.	
IV.	Proof of claim verified November 30, 1934, by Milton L. Masson, Special Deputy Superintendent of Banks, being in substance a claim for the rights and equities assigned to or reserved by The Prudence Company, Inc., under agreement of April 9, 1920.	No amount stated
95 V.	Proof of claim verified November 30, 1934, by Milton L. Masson, Special Deputy Superintendent of Banks, being in substance a claim for (a) sums advanced by The Prudence Company, Inc. for the protection of the Trust Funds and the mortgages, subject to the Certificate Issues, and (b) sums paid by The Prudence Company, Inc. under its guarantees of Prudence bonds and Prudence Certificates, and (c) all other rights arising upon said guarantees.	$1,512,788.52
96 VI.	Proof of claim verified November 30, 1934, by Milton L. Masson, Special Deputy Superintendent of Banks, being in substance a claim for Prudence certificates deposited by The Prudence Company, Inc. as security for certain guarantees of The Prudence Company, Inc. to Realty Associates Securities Corporation.	48,000.00

except in so far as any of the foregoing proofs of claim may constitute a claim in and to the uncertificated portions of certain certificated mortgages more fully described hereafter. Without limiting the generality of the foregoing, it is our intention to release any claim we may have to so-called "unissued bonds", i.e., bonds which might have been issued against an excess of collateral in any one of the eighteen bond issues over the then outstanding face amount of bonds previously issued, and it is our intention to withdraw any claim in and for such unissued bonds and any and all other claims not expressly reserved herein and all our rights, liens and interests with respect thereto against Prudence-Bonds Corporation and its estate including its pledged collateral. 98

(4) We will execute consents to the pending plans of reorganization of the eighteen series of Prudence-Bonds which have been heretofore approved by the Special Master and to the amended general plan of reorganization dated March 24, 1937.

(5) We will withdraw any and all answers, exceptions or objections heretofore filed by us to the Debtor's amended plan of reorganization dated March 24, 1937, to the report of Hon. James G. Moore as Special Master thereon, dated March 11, 1937, as amended by letter dated March 24, 1937 from said Special Master to the court, and any and all objections or exceptions to the motions to confirm the said report of the said Special Master or the said plan of reorganization. 99

(6) We will withdraw any and all answers, exceptions or objections heretofore filed by us or on our behalf to the motions to confirm the several plans of reorganization of the eighteen series of Prudence-Bonds which may have been made heretofore and any and all exceptions to the report

100 *Exhibit "C":*

or reports of Hon. James G. Moore, with respect to such plans of reorganization.

(7) Our counsel will withdraw their petition heretofore filed for fees and allowances in connection with hearings on the "parity issue", and make no claim of any kind in the Seneca Issue of mortgage participation certificates or its plan of reorganization, and neither we nor our counsel will make any application or claim for fees and allowances in connection with any of the separate plans of reorganization of the eighteen series of Prudence-Bonds, the Seneca Issue of mortgage participation certificates, the amended general plan of reorganization, nor in connection with the
101 entire proceedings for the reorganization of Prudence-Bonds Corporation. We expressly reserve our claims on behalf of the Estate of The Prudence Company, Inc. for reimbursement of the cost and expenses of servicing and administering the collateral underlying the eighteen series of Prudence Bonds.

In return for all of the foregoing, we are to receive a sum equal to 50% of all moneys heretofore set aside, segregated or reserved at the time distribution or distributions were made to other holders of the said bonds, provided, however, that the aggregate of such sums to be paid to us shall not exceed the sum of $150,000., and we will release any and all claims which we may have to the balance of such segregated funds. The source from which said pay-
102 ment is to be made shall be subject to the order of the Court in your proceedings.

(8) We are to receive any and all right, title and interest of Prudence-Bonds Corporation or yourselves in and to those certificated mortgages against which certificates have been issued by Prudence-Bonds Corporation and of which Prudence-Bonds Corporation is the owner and holder, or which Prudence-Bonds Corporation has deposited with a depositary for the issuance of Prudence mortgage par-

ticipation certificates, in so far as the said mortgages have not been certificated or in so far as no certificates have been issued against any portion of such mortgages. It is understood that the face amount of such uncertificated portions of such mortgages is $156,450.64. We are to receive the said uncertificated or unissued portions of the said mortgages subject to the claims of any general creditors of Prudence-Bonds Corporation.

(9) Nothing herein contained shall in any way affect or subordinate bonds of the eighteen series of Prudence-Bonds held by us as collateral for loans made by The Prudence Company, Inc. under the terms of collateral notes and which are held by us in pledge. 104

(10) You and we agree to execute any and all documents and papers necessary to effectuate any of the foregoing, including a general release in usual form to be executed by us releasing Prudence-Bonds Corporation and you of and from all claims, liens, rights or interests which we may now have and which are not specifically reserved herein.

Nothing herein contained or the execution or consummation of this agreement is in any way to affect, vary, impair or increase the rights of bondholders of the eighteen series of Prudence-Bonds with respect to the guarantee thereof made by The Prudence Company, Inc.

If the foregoing terms are acceptable to you, will you please acknowledge such acceptance by letter addressed 105 to us, referring to this letter and to the terms of the offer contained herein.

Very truly yours,

STEPHEN CALLAGHAN
JOHN M. McGRATH
WILLIAM T. COWIN
As Trustees of The Prudence
Company, Inc., Debtor.

JJF:PA

106 *Exhibit "C".*

EXHIBIT B

December 13, 1937.

Stephen Callaghan, John M. McGrath
and William T. Cowin, Trustees of
The Prudence Company, Inc.,
331 Madison Avenue,
New York City, N. Y.

Dear Sirs:—

The undersigned are this day in receipt of your letter
107 dated December 9, 1937, setting forth the terms of an offer of settlement of the various claims, including Parity and other matters.

We accept the said offer, subject to the approval of the Court having jurisdiction in both of our proceedings.

Very truly yours,

CHARLES H. KELBY
CLIFFORD S. KELSEY
Trustees of Prudence-Bonds Corporation.

108

Exhibit "C". 109

UNITED STATES DISTRICT COURT,

EASTERN DISTRICT OF NEW YORK.

IN THE MATTER

OF

THE PRUDENCE COMPANY, INC.,

Debtor.

In Consolidated Proceedings for Reorganization under Section 77B of the Bankruptcy Act.

Nos. 27496 and 27028.

In the Matter of the Application of the Trustees of the Debtor for an order approving a settlement and compromise of the claims of the estate of The Prudence Company, Inc. against Prudence-Bonds Corporation and its estate, and authorizing and directing the settlement and compromise of the same.

110

A motion by an order to show cause signed by the Hon. Grover M. Moscowitz and dated December 15, 1937, upon the petition of Stephen Callaghan, John M. McGrath and William T. Cowin, duly verified the 15th day of December, 1937, with exhibits thereto attached, and upon all the papers filed and proceedings heretofore had herein, having duly come on to be heard before me on the 30th day of December, 1937 for an order herein: 111

(a) Approving an agreement of settlement between the aforesaid Trustees of the Debtor and Charles H. Kelby and Clifford S. Kelsey, Trustees of Prudence-Bonds Corporation, Debtor; and

(b) Authorizing and empowering the said Trustees of the Debtor to carry out the said settlement agreement; and

112 *Exhibit "C".*

(c) Authorizing and empowering the said Trustees of the Debtor herein to do all acts necessary and to execute all papers, documents or other instruments in writing proper and necessary to carry out the said settlement agreement; and

(d) For such other and further relief as might be proper in the premises;

Now, upon all the papers and proceedings heretofore had herein and upon reading and filing the said order to show cause and said petition of Stephen Callaghan, John M. McGrath and William T. Cowin, Trustees of the Debtor
113 herein, duly verified the 15th day of December, 1937, and exhibits thereto attached, with proof of due service thereof upon the necessary parties to this proceeding and proof of due publication of the notice to creditors and stockholders of the Debtor of said hearing, all as required by said order to show cause, and after hearing Thomas Cradock Hughes and Emanuel Celler (Samuel S. Allan, Esq., of counsel), solicitors for the Trustees of the Debtor, in support thereof, and no one appearing in opposition thereto, and due deliberation having been had thereon, it is

ON MOTION of THOMAS CRADOCK HUGHES and EMANUEL CELLER, solicitors for the Trustees of the Debtor herein, hereby

114 ORDERED, ADJUDGED AND DECREED AS FOLLOWS:

(1) That by virtue of the due service of said order to show cause and petition, and due publication of the notice to creditors and stockholders of the Debtor, as above described, the Debtor and all persons interested in the Debtor, whether as creditors and stockholders or otherwise, are adequately represented in this proceeding, as required by law, so as to cause the decree herein to be binding upon each and every one of them;

(2) That the settlement and compromise of the claims of The Prudence Company, Inc. and its Trustees against Prudence-Bonds Corporation upon the terms and conditions set forth in the agreement of settlement annexed as an exhibit to said petition of the Trustees of the Debtor be and the same hereby is in all respects authorized and approved;

(3) The Trustees of the Debtor are hereby authorized and empowered to consent to the eighteen approved Plans of Reorganization for the eighteen series of bonds of Prudence-Bonds Corporation and to the approved Amended General Plan of Reorganization of Prudence-Bonds Corporation. 116

(4) The Trustees of the Debtor are hereby authorized and empowered to submit the bonds of the said eighteen series of Prudence-Bonds owned by said Trustees for stamping with an appropriate legend indicating that they are subordinate as provided for in the said eighteen Amended Plans of Reorganization and as defined by an order made by Hon. Robert A. Inch, a Judge of this Court, on July 21, 1937 in proceedings for the reorganization of Prudence-Bonds Corporation.

(5) The Trustees of the Debtor are authorized to withdraw and discontinue the appeal heretofore prosecuted by them from the said order of July 21, 1937 to the Circuit Court of Appeals for the Second Circuit.

117

(6) The said Trustees of the Debtor are hereby authorized and empowered to withdraw the proofs of claim and claims agreed to be withdrawn in said settlement agreement but only to the extent provided for in said settlement agreement.

(7) The Trustees of the Debtor are authorized and empowered to withdraw any answers, exceptions or objections heretofore filed by them or on their behalf to the eighteen

approved Plans of Reorganization of the eighteen series of Prudence-Bonds or to the respective Reports of Special Master James G. Moore, thereon, or to the motions to confirm said Plans and Reports or to the approved Amended Plan of Reorganization of Prudence-Bonds Corporation dated March 24, 1937, or to the Report of Hon. James G. Moore as Special Master thereon, or to the motion to confirm said Plan and Report.

(8) The said Trustees of the Debtor and their counsel, Thomas Cradock Hughes and Emanuel Celler, are authorized to withdraw their application for fees and allowances heretofore filed before Hon. James G. Moore as
119 Special Master in the proceedings for the reorganization of Prudence-Bonds Corporation, in connection with hearings to determine the status of Prudence-Bonds of the eighteen series of Prudence-Bonds Corporation owned and held by said Trustees of The Prudence Company, Inc.

(9) The said Trustees of the Debtor are authorized and directed upon the consummation of the settlement to turn over and pay to the respective corporate trustees of the eighteen issues of Prudence-Bonds any and all moneys heretofore set aside, reserved or segregated for distribution by said Trustees on account of the Prudence-Bonds of the said eighteen series owned by said Trustees, and to furnish to said corporate trustees and each of them any and all statements, accountings or information necessary
120 in connection therewith provided, however, that said Trustees shall receive the sum provided to be paid to them by said settlement.

(10) The said Trustees are further authorized to execute any further documents, releases or instruments and to do all things necessary and proper to perfect and carry out the terms of the said settlement agreement.

Dated: Brooklyn, New York, January 28th, 1938.

GROVER M. MOSCOWITZ,
U. S. D. J.

121

EXHIBIT "D"

United States District Court

Eastern District of New York

IN THE MATTER

OF

THE PRUDENCE COMPANY, INC.,

DEBTOR. 122

IN THE MATTER OF THE GENERAL PLAN OF REORGANIZATION PROPOSED BY RECONSTRUCTION FINANCE CORPORATION.

In Consolidated Proceedings for Reorganization under Section 77B of the Bankruptcy Act.

Nos. 27496 and 27028.

123

ORDER, DATED MAY 26, 1939, RELATIVE TO AMENDMENTS, CONFIRMATION, CONSUMMATION AND OTHER MATTERS.

AMENDED

PLAN OF REORGANIZATION

for

THE PRUDENCE COMPANY, INC.

As Proposed by Reconstruction Finance Corporation, April 12, 1938, with Amendments, and as Confirmed by Order of the Court dated May 26, 1939.

In Consolidated Proceedings Nos. 27496 and 27028 in the District Court of the United States for the Eastern District of New York for the Reorganization of The Prudence Company, Inc., under Section 77B of the National Bankruptcy Act.

than in respect of capital stock) consist mainly of the amount due in respect of the note payable held by the RFC, and amounts due on guarantees of whole mortgages and of Prudence-Bonds Corporation secured bonds and mortgage participation certificates.

From information furnished by the Section 77B Trustee as at the confirmation of the Plan, the claims filed against the Debtor (after deduction for such thereof, including Federal income tax claims and New York State franchise tax claims, as have been withdrawn, released, settled or paid, or separately reorganized or finally disallowed in these proceedings, or ordered so to be, or as are payable out of segregated funds) may be summarized, approximately, as follows, including interest except as noted:

Nature of Claim	*Amount*
(1) Claim of the RFC	$ 11,848,000*
(2) Claims arising out of guarantees by the Debtor of obligations of others:	
(a) Guarantees of Prudence-Bonds Corporation secured bonds (excludes Debtor-owned bonds)	58,833,000†
(b) Guarantees of Prudence-Bonds Corporation mortgage participation certificates (excludes Debtor-owned certificates)	50,858,000†
(c) Guarantees of whole mortgages	12,523,000
(3) Miscellaneous claims	151,000‡
Total	$134,213,000§

There being no feasible way of reorganizing the Debtor as a going concern with a continuing business, the object of the Plan is to facilitate the most advantageous realization of the assets and the most equitable distribution of their

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* Upon consummation of the Plan the RFC's claim is to stand allowed in the reduced amount of approximately $11,348,000—see Plan, Article IV, (3h).

† Excludes the 1111 Park Avenue, Park Place Dodge, 100 West 55th Street and Blind Brook issues (fully paid), and the Wortheo and Dryden issues (released).

‡ Excludes Manufacturers Trust Company's claim, settlement of which without payment out of the Debtor's general assets was pending before the Court when the Plan was confirmed.

§ Does not reflect the above mentioned reduction to be made in the RFC's claim.

proceeds to the creditors. As indicated above, the major portion of the claims against the Debtor arises out of guarantees of whole mortgages and of Prudence-Bonds Corporation secured bonds and mortgage participation certificates. Because of uncertainties in the real estate market it is impossible to tell at this time which bond and certificate issues and which whole mortgages may ultimately be paid in full (with or without a surplus) and which ones may result in a deficiency. It is also believed that the nature of the assets in the Debtor's estate is such that a substantial sacrifice of values would result if the assets were liquidated under the limitations and handicaps necessarily incident to bankruptcy proceedings.

In the light of these considerations, the Plan contemplates the reorganization of the Debtor so as to provide, through the medium of a business organization, for an orderly realization of assets and for a distribution of the proceeds in cash among the Participants in the Plan (as therein defined) in such manner as to take equitable account of the substantial variations in the extent to which they are secured.

With a view to the making of as large and immediate a cash payment as reasonably practicable to the main group of creditors other than the RFC, the Plan, as more fully set forth in Article IV thereof, provides that the RFC will forego, until the Final Distribution under the Plan, its share of the initial cash distribution, thus in effect advancing such cash, without interest, for distribution among the Secured Participants (as defined in Article I of the Plan), such Participants consisting chiefly of holders of claims based on the Debtor's guarantee of whole mortgages and of Prudence-Bonds Corporation secured bonds and mortgage participation certificates.

For the purpose of computing the amounts to be thus initially distributed to Secured Participants, such Participants are not required by the Plan to make any offset against the amount of their claims in respect of the value of the security held by them. As to subsequent distribu-

tions, the Plan provides in effect that in computing the amounts to be distributed, there shall be an offset against the Secured Participants' claims to the extent of the value (to be determined as provided in Article V of the Plan) of any security held for their claims (or for the obligations to which their claims relate) whether such security relates to property owned by the Debtor or a third party, an exception being made to the foregoing if such third party is a guarantor or surety for the Debtor,—this because the reduction of any claim against the Debtor by the amount realized against the guarantor or surety would merely give rise to a corresponding claim on his part against the Debtor.

From the inception of these proceedings up to July 6, 1937, the RFC was enjoined from realizing upon its security, and thereafter the RFC refrained from so doing pending negotiations with the Section 77B Trustees with a view to effecting a realization in such a way as to yield the maximum benefit to all creditors. As a result of these negotiations all of the collateral pledged by the Debtor with the RFC has been sold, under supervision of the Court, and pursuant to orders of the Court providing for certain minimum bids for substantially all of such collateral. The RFC was the sole and exclusive bidder for such collateral by virtue of its bids aggregating approximately $11,323,000. As a result of such sale the RFC is an Unsecured Participant under the Plan as therein defined, and will therefore share in the initial cash distribution only on the basis of its reduced claim, whereas the Secured Participants will share in such distribution without offsetting to any extent the value of their security.

The Judge in these proceedings having found by order dated April 25, 1938, that the Debtor is insolvent, the Plan makes no provision for the stockholders of the Debtor.

AMENDED PLAN OF REORGANIZATION

for

THE PRUDENCE COMPANY, INC.

ARTICLE I.

DEFINITIONS.

In this Plan the following terms have the following meanings unless otherwise expressly stated:

Debtor means The Prudence Company, Inc.

Section 77B means Section 77B of the National Bankruptcy Act, including all amendments to date.

Court means the United States District Court for the Eastern District of New York acting in the proceedings under Section 77B with respect to the Debtor.

Section 77B Trustee means the Trustee of the Debtor appointed by the Court.

Plan means this Plan of Reorganization.

Effective Date means the date as of which the Plan is consummated pursuant to the order of the Court.

Record Date means any record date fixed by the Court or otherwise as provided in the Plan, for any appropriate purpose of the Plan.

New Company means the new corporation in which the assets and business of the Debtor's estate are to be vested pursuant to Article III of the Plan.

Creditors means "creditors" as defined in Section 77B(b).

Claims means "claims" as defined in Section 77B(b).

Collateral means (1) the bonds and mortgages and other property, tangible or intangible, real or personal, held as security for any one of the eighteen separate bond issues of Prudence-Bonds Corporation guaranteed by the Debtor; (2) any bond and mortgage or other property, tangible or intangible, real or personal, in which certificates of participation have been issued by Prudence-Bonds Corporation and guaranteed by the Debtor, or any bond

and mortgage or other property, tangible or intangible, real or personal, securing any such certificates of participation or securing any bonds or certificates or other securities issued or received in exchange for or in lieu of such certificates of participation; (3) any whole single bond and mortgage or interest therein, guaranteed by the Debtor (other than bonds and mortgages, and interests therein, referred to in clauses (1) and (2) of this definition) or property, tangible or intangible, real or personal, acquired upon foreclosure thereof or by deed in lieu thereof or in exchange for such bond and mortgage, or interest therein, or for any such property, and in case of the sale of property so acquired, any purchase money bond and mortgage on such property taken back on such sale by the mortgagee.

Participant means a holder of a finally allowed claim against the Debtor upon which claim the Debtor is personally liable. Unless otherwise indicated by the context such term shall be deemed to include the assignee of a Participant claiming under a valid assignment in writing duly filed with the Section 77B Trustee or the New Company as the circumstances of the case may reasonably require.

Secured Participant means a Participant whose claim (or the obligation to which his claim relates) was secured on February 1, 1935, by either (a) Collateral, or (b) security other than Collateral (unless such other security consisted of property or an obligation of a guarantor of or surety for the Debtor in respect of such claim); provided, however, that no Participant who (or whose predecessor in interest) held, on February 1, 1935, security of the character referred to in the foregoing subdivision (b) which security, prior to the Effective Date, has been sold or realized upon in its entirety, shall be deemed a Secured Participant. No property acquired by a Participant (or his predecessor in interest) prior to February 1, 1935, through the entire foreclosure of a Single Mortgage, as hereinafter defined, shall be deemed to have been held on February 1, 1935, as security for such Participant's claim based upon

the guarantee by the Debtor of such Single Mortgage, and such Participant shall not be deemed a Secured Participant with respect to such claim. Each Prudence Bond Participant and Prudence Certificate Participant, as hereinafter respectively defined, shall be deemed a Secured Participant.

Unsecured Participant means a Participant who is not a Secured Participant.

RFC means Reconstruction Finance Corporation, its successors and assigns.

Prudence Bond means any bond issued by Prudence-Bonds Corporation and guaranteed by the Debtor.

Prudence Certificate means any certificate of participation in a bond and mortgage issued by Prudence-Bonds Corporation and guaranteed by the Debtor.

Single Mortgage means any bond and mortgage or interest therein guaranteed by the Debtor other than (a) any bond and mortgage in respect of which Prudence Certificates have been issued, or (b) any bond and mortgage constituting part of the Collateral securing any issue of Prudence Bonds.

Prudence Bond Participant means a Participant whose claim is based on the guarantee by the Debtor of a Prudence Bond.

Prudence Certificate Participant means a Participant whose claim is based on the guarantee by the Debtor of a Prudence Certificate or of a bond and mortgage as to which Prudence Certificates have been issued.

Reserved Right Participant means a person who, between February 1, 1935 and the Effective Date, disposed of his Prudence Bond or Prudence Certificate (or of an instrument representing a beneficial interest therein, such as, but not necessarily limited to, a Trustee's certificate) and who, by proof filed with the Clerk of the Court on or before July 15, 1939, establishes to the Court's satisfaction that, upon such disposition, he reserved to himself the rights against the Debtor based upon the Debtor's guarantee of such Prudence Bond or Prudence Certificate.

New Company's Register means the register to be kept by the New Company as provided in paragraph 3(e) of Article IV hereof.

Appraisers means the appraisers selected to value the Collateral and other security as provided in Article V hereof.

New Loan Value of a parcel of real estate means the amount of money which, in the sworn opinion of the Appraisers, on the basis of the appraised value of such real estate arrived at as provided in Article V hereof, would constitute at the Effective Date a reasonable new first mortgage loan on such real estate, at the rate of interest and upon the terms found by the Appraisers to be then current for such loans; provided, however, that unless all three Appraisers agree that such New Loan Value is less than two-thirds of such appraised value, such New Loan Value shall be fixed at not less than two-thirds of such appraised value.

The phrase *obligation to which a claim relates* or its substantial equivalent means the obligation, or interest therein, on which (or on the guarantee of which), such claim is based and shall be deemed to include any obligation or interest therein issued in lieu of, or in exchange for, such obligation or interest therein.

ARTICLE II.

Parties Not Affected by the Plan.

Creditors whose claims against the Debtor have, prior to the Effective Date, been paid in full, or expressly withdrawn, released or compromised, or expunged by order of the Court, are not affected by the Plan and the Plan makes no provision for them. These creditors include the holders of the Debtor's Guaranteed Collateral Trust 5½% Gold Bonds, due May 1, 1961, of the Debtor's First Mortgage Group Certificates, Series B, and of the so-called Worthco.

Dryden, 1111 Park Avenue, Park Place Dodge, 100 West 55th Street and Blind Brook issues of Prudence Certificates.

The assets of the Debtor which are subject to claims for which the Debtor is not personally liable are to be vested in the New Company subject to such claims; accordingly, no separate or additional provision is made in the Plan with respect to the holders of such claims and they are not affected by the Plan.

The Judge in these proceedings having found by order dated April 25, 1938, that the Debtor is insolvent, the stockholders of the Debtor are not affected by the Plan and the Plan makes no provision for them.

ARTICLE III.

The New Company.

On the Effective Date, or as soon thereafter as practicable, the business conducted at the time being by the Section 77B Trustee and all assets of whatever nature in the Debtor's estate shall be vested in a new corporation, to be formed for the purpose (i. e., the New Company) free and clear of all claims and interests of the Debtor, its stockholders and creditors, and others, except the following which shall remain outstanding:

(1) such tax or other finally allowed claims, if any, as the Court may determine to have priority, and the items provided for in Article VIII hereof,

(2) finally allowed claims against the property of the Debtor in respect of which the Debtor is not personally liable, and

(3) finally allowed claims of the character which shall entitle the holders thereof to be deemed Participants as defined in Article I hereof;

provided, however, that all causes of action or rights in the Debtor's estate against present or former officers or

directors of the Debtor, and against other parties arising out of or relating to the transactions giving rise to such causes of action or rights, shall remain in the Section 77B Trustee, subject to being vested in the New Company when so ordered by the Court; pending such order, such causes of action or rights shall be prosecuted or otherwise disposed of for the benefit of the New Company in such manner as the Section 77B Trustee, with the approval of the Court, shall determine. All expenses of such prosecution or other disposition shall be borne by the New Company, subject to order of the Court, and the net proceeds thereof shall be paid to the New Company.

As sole consideration for the vesting of such business and assets in the New Company as aforesaid, the New Company shall issue all of its authorized capital stock as hereinafter in this Article III more fully provided.

The claims referred to in the foregoing subdivision (2) shall be payable only out of the property against which they are claims.

The claims and items referred to in the foregoing subdivisions (1) and (3) shall be paid by the New Company, but only as follows:

The claims and items referred to in the foregoing subdivision (1) shall be paid in full in due course out of the New Company's assets. Such claims and items shall not constitute liens upon such assets, but shall have priority over all distribution to Participants under the Plan and over all liabilities incurred by the New Company; and the New Company shall be entitled to sell all or any part of such assets free and clear of any charge in respect of such claims and items.

The claims referred to in the foregoing subdivision (3) shall not constitute liens upon the New Company's assets, and the New Company shall be entitled to sell all or any part of such assets free and clear of any charge in respect of such claims; provided, however, that nothing herein contained shall be deemed to affect the lien, if any, to which any part of such assets was subject, immediately prior

to the vesting thereof in the New Company, in respect of any such claim. The claims referred to in such subdivision (3) shall be payable, without interest, only as provided in Article IV hereof and only to the extent that the New Company's assets shall be sufficient to pay them, after reserving from such assets $70 for the New Company's capital and $70 for its surplus, and after payment of or provision for (i) the claims and items referred to in the foregoing subdivision (1) and (ii) such liabilities as may be incurred by the New Company. Such surplus shall be available to pay for stock which may be purchased by the New Company under the options hereinafter in this Article III provided for.

The name of the New Company shall be "Prudence Realization Corporation" or such other name as the Court may approve. The New Company shall not engage directly or indirectly in any business other than the business of administering, conserving and realizing upon its assets in an orderly manner, and of conducting the "servicing" and any other business activities that (a) are vested in the New Company as herein provided, or (b) may be undertaken by the New Company, upon vote of its Board of Directors, with respect to Prudence Bonds, Prudence Certificates and Single Mortgages, or securities or mortgages or interests therein issued in exchange therefor, or in payment or part payment thereof, or in lieu thereof; provided, however, that the foregoing restrictions shall in no way impair or otherwise affect the validity or binding effect of any transaction within the scope of the purposes, objects and powers set forth in the New Company's certificate of incorporation or entered into by the New Company in the exercise of any power, right or privilege vested in it by law, and provided, further, that if any question shall otherwise arise as to whether any activity of the New Company exceeds such restrictions, the judgment of the Board of Directors, evidenced by a resolution thereof concurred in by directors of each class, shall be conclusive in the absence of a showing of bad faith.

Appropriate steps shall be taken for the incorporation of the New Company as a stock corporation under the laws of the State of New York, with an authorized capital stock consisting of seven shares of capital stock without par value, of which five shares shall be designated as Class A Stock and two shares as Class B Stock.

The entire authorized capital stock of the New Company shall be issued, and such stock, together with all dividends and distributions in respect thereof, shall be held and disposed of, as in this Article III and in Article IV set forth. No dividend or other distribution shall be paid or made upon or in respect of the New Company's capital stock until all Participants become Paid-Up Participants as defined in paragraph 3(a) of Article IV hereof, and each such share of stock shall be subject to repurchase by the New Company from the holder thereof upon vote of its Board of Directors concurred in by not less than five directors, including at least one Class B director.

The Board of Directors of the New Company shall consist of seven directors, of whom five shall be designated as Class A directors and two shall be designated as Class B directors. After the designation of the initial directors of the New Company as hereinafter provided, the Class A Stock shall be entitled to elect the Class A directors and the Class B Stock shall be entitled to elect the Class B directors. Cumulative voting shall be provided for so that each share of Class A Stock shall be entitled to elect one Class A director and each share of Class B Stock shall be entitled to elect one Class B director. Except as aforesaid, there shall be no distinction between the Class A Stock and the Class B Stock. With the unanimous approval of the directors then in office, the Board of Directors may provide for an Executive Committee of the Board. A majority of such Committee shall be Class A directors and one member thereof shall be a Class B director.

The initial directors shall be designated as follows:

(a) Four of the initial Class A directors shall be designated by the Court. On or before such date as the Court may determine, creditors (other than the RFC) may file with the Court written suggestions as to persons to act as such four Class A directors, but the Court shall be free to make each such designation without regard to whether the name of the person so designated has been so suggested.

(b) Each creditor holding a claim in respect of a Prudence Bond, Prudence Certificate or Single Mortgage shall be entitled to file with the Section 77B Trustee, at any time prior to the confirmation of the Plan or such earlier date as the Court may fix, his written nomination of the remaining Class A director. The person so nominated by the creditors holding in the aggregate the largest principal amount of such claims shall be deemed designated as such Class A director.

(c) The initial Class B directors shall be designated by the RFC.

The certificate of incorporation or the by-laws of the New Company shall provide, in effect, that to qualify as such from and after the Effective Date, directors shall be stockholders.

The entire capital stock of the New Company (to consist, as aforesaid, of five shares of Class A Stock and two shares of Class B Stock) shall be issued to the Section 77B Trustee acting on behalf of the Debtor, as sole consideration for and upon the transfer to and the vesting in the New Company of the business and assets of the Debtor's estate as above provided in this Article III. The Section 77B Trustee shall forthwith upon the issuance of said stock assign and transfer one share of Class A Stock to each of the five initial Class A directors and one share of Class B Stock to each of the two initial Class B directors. Upon the receipt of such stock and in consideration for the transfer and assignment thereof to him, each such person shall enter into a written agreement with the New

Company to the effect that he accepts the same for the purposes and subject to the restrictions of the Plan and subject to the option of the New Company to repurchase such share at any time upon the payment to him of the sum of $10.00, and that throughout his term of office he will continue to hold such share. Each such person shall also agree to and shall endorse the certificate for his share of stock in blank and deposit the same with the New Company as security for the performance of such agreement.

Beginning with the year following the Effective Date, annual meetings of the stockholders shall be held for the purpose of electing directors. Each holder of a share of Class A Stock shall be entitled, in his discretion, to vote such stock for the election of himself as a Class A director, and each holder of a share of Class B Stock shall be entitled, in his discretion, to vote such stock for the election of himself as a Class B director. The certificate of incorporation of the New Company shall provide, in effect, that if any vacancy shall occur in the office of a Class A director, his successor shall be elected by the remaining holders of the Class A Stock, and that if any vacancy shall occur in the office of a Class B director, his successor shall be elected by the remaining holder of the Class B Stock; provided, however, that if any such vacancy shall not be so filled within the thirty days following its occurrence, such vacancy may be filled by a majority vote of the holders of all the issued and outstanding stock of the New Company, without distinction between Class A Stock and Class B Stock and without cumulative voting. If the offices of both Class B directors shall be vacant at any one time, the RFC (or its assignee on the New Company's Register) shall be entitled, within the thirty days following the occurrence of the second vacancy, to nominate the persons to be elected as the succeeding Class B directors; and appropriate provision to this effect shall be made in the written agreements to be entered into between the New Company and the holders

of Class A Stock pursuant to the foregoing paragraph of this Article III.

If any director shall cease to be such, by virtue of his death, resignation, failure of re-election, or otherwise, the New Company shall exercise its option, hereinabove provided for, to purchase the share of stock of the New Company theretofore held by such director. In such event, or in the event that the New Company shall for any other reason have repurchased a share of stock from any director, as hereinabove provided, and his office shall have become vacant because of his resulting disqualification, the share of stock so acquired by the New Company shall be transferred to the person elected to fill such vacancy, against payment to the New Company of the sum of $10.00, and such person shall thereupon enter into a written agreement with the New Company with respect to such stock to the same effect as the agreement made by his predecessor with the New Company, and shall also agree to and shall endorse the certificate for such share in blank and deposit the same with the New Company as security for the performance of his said agreement.

Except as otherwise provided in the Plan, the Board of Directors of the New Company shall act by a majority vote of a quorum which shall consist of not less than four directors. Each director shall be entitled to compensation not exceeding $1200 per annum, but, by vote of the Board of Directors concurred in by at least one director of each class, additional compensation may be paid to any director for his services as an officer of the New Company or for other special services. The aggregate compensation paid to the principal officers of the New Company during the first year following the Effective Date shall not exceed an amount approved by the Court as fair and reasonable.

Within three months after the close of each fiscal year, the Board of Directors shall cause a certified public accountant or a firm of certified public accountants selected by it, to examine the books and records of the New Com-

pany, and to submit to the Board of Directors a report which shall include a financial statement with respect to the operations of the New Company and its distributions to Participants during such fiscal year, and a balance sheet as of the close of such fiscal year. The New Company shall keep such report on file, open to the inspection of any Participant during reasonable business hours.

Upon completion by the New Company of the realization of all its assets and the distribution in cash among the Participants of the net proceeds thereof as more fully provided in Article IV hereof, the Board of Directors of the New Company shall take such action as shall be appropriate to terminate the corporate existence of the New Company and to surrender and cancel all the stock of the New Company.

ARTICLE IV:

Disposition of the New Company's Assets.

1. *Initial Distribution of Cash.* As soon as practicable after the Effective Date, the cash vested in the New Company as provided in Article III hereof (over and above such amount as may be retained by the New Company, with the approval of the Court, for current expenses and for the claims and items referred to in subdivision (1) of Article III hereof) shall be distributed among the Participants *pro rata* subject to the conditions set forth in this Article IV; provided, however, that the amount of cash which the RFC would be entitled to receive upon such *pro rata* distribution shall be distributed among the Secured Participants, and provided further, that for the purpose of computing the amount of any distribution to be made under this paragraph 1 no offset shall be made against the amount of the claim of any Secured Participant in respect of the value of the Collateral or other security securing his claim or the obligation to which his claim relates.

2. *Realization of Assets and Subsequent Distributions to Participants.* The New Company shall proceed, as promptly as deemed advisable by its Board of Directors in the interests of the Participants, with an orderly realization of its assets and the eventual reduction thereof to cash.

From time to time and subject to the conditions hereinafter in this Article IV set forth, the New Company shall distribute such cash (after making payment of or appropriate provision for its expenses and liabilities) *pro rata* among the Participants until all the Participants become Paid-Up Participants as defined in paragraph 3(a) of this Article IV; provided, however, that

(i) no distribution shall be made, prior to the Final Distribution referred to in subdivision (iv) below, unless the cash available therefor shall amount to at least $250,000;

(ii) except as otherwise expressly provided for in clause *First* of subdivision (iv) below, each Participant, for the purpose of all distributions under this paragraph 2, shall be entitled to participate in the proportion that (a) his claim, minus the applicable deductions provided for below in this subdivision (ii), bears to (b) the total claims of all Participants, minus the aggregate of such deductions; the said deductions to be made from the claim of each Secured Participant for such purpose to consist of (1) the *pro rata* value (determined pursuant to Article V hereof) of all Collateral or other security securing his claim or the obligation to which his claim relates, plus (2) the *pro rata* share of the total amount of cash received or realized subsequent to February 1, 1935 (the date as of which the Court approved the Debtor's petition for reorganization) and prior to the Effective Date in respect of the principal amount or corpus of any Collateral or other security which, at any time during such period, secured his claim or the obligation to which his claim relates, such cash deduction to include, in case such obligation has been purchased by a sinking or retirement fund, the amount of cash paid

in respect of such principal amount or corpus upon such purchase; provided, however, that

(a) if, in the judgment of the Board of Directors, no definitive proration should be made of the value of the Collateral or other security for a particular certificate issue, due to uncertainty whether certificates of such issue held in the Debtor's estate on the Effective Date are on a parity with other certificates of such issue, the deduction to be made pursuant to the foregoing clause (1) shall be based in the first instance on the assumption that the certificates so held in the Debtor's estate are not entitled to parity, and an appropriate reserve shall be established by the New Company to provide for the additional distribution to be made to certificate holders of such issue if the Board of Directors shall be later satisfied that such parity exists; the Board of Directors being authorized to discontinue such reserve if and when satisfied that such parity does not exist;

(b) in determining whether or not any cash received or realized as specified in the foregoing clause (2) was in respect of principal, the New Company may rely upon the designation made, in connection with the payment thereof, by the payor or distributing agent, or if no designation was so made, then upon any designation made by an order of any court having jurisdiction in the premises or by the provisions of any applicable consummated plan of reorganization, or, in the absence of any such designation, upon the advice of counsel; and

(c) no cash shall be deemed to have been so received or realized, upon a foreclosure sale, by the owner of the lien foreclosed, or an interest therein, if and to the extent that his distributive share of the proceeds of such sale were applied by him in payment for the property sold or an interest therein;

(iii) prior to such Final Distribution, no distribution shall be made under this paragraph 2 unless after such distribution there will remain in the New Company assets which have, in the judgment of the Board of Directors (concurred in by directors of both

classes), a realizable cash value of at least twice (a) the amount of the RFC's share in the initial cash distribution which was distributed to the Secured Participants pursuant to paragraph 1 of this Article IV, plus (b) an amount sufficient to pay all expenses and liabilities of the New Company theretofore and thereafter to be incurred;

(iv) when the assets of the New Company have been reduced to such an extent that, due to the limitations of the foregoing subdivision (iii), no distribution other than the Final Distribution can be made, the New Company shall proceed as promptly as practicable with the realization of such assets, and from time to time as cash becomes available shall make distributions as follows, the last such distribution to include the amounts theretofore reserved by the New Company in respect of its capital and surplus (all distributions made under this subdivision (iv) being collectively designated as the Final Distribution):

First: To the RFC, until the RFC shall have received (from the Final Distribution) the same percentage on its claim as the Secured Participants shall theretofore have received under the Plan upon their respective unreduced claims from the initial distribution provided for in paragraph 1 of this Article IV.

Second: After making appropriate provision for the actual and estimated expenses and liabilities of the New Company theretofore and thereafter to be incurred, *pro rata* to all Participants, including the RFC.

If and when all Participants become Paid-Up Participants as defined in paragraph 3(a) of this Article IV, any remaining proceeds of the realization of the New Company's assets not required to meet its actual and estimated expenses and liabilities theretofore and thereafter to be incurred shall be distributed upon the New Company's stock; and the then directors of the New Company who, as stockholders, shall be entitled to receive the amount so distributed shall forthwith cause such amount to be dis-

tributed among the Participants in the manner and subject to the conditions provided in this paragraph 2 and in the following paragraph 3 of this Article IV.

3. *General Conditions Relative to Distributions.* The following shall apply to all distributions made pursuant to this Article IV:

(a) When from all sources (whether from the New Company or otherwise) the full amount of a Participant's claim, as finally allowed in these proceedings, shall have been realized in cash in respect of the obligation to which such claim relates (or in respect of any property acquired either in connection with the collection of such claim or obligation, or by deed in lieu of foreclosure, or in exchange for any such obligation or any property so acquired) such Participant shall be deemed a Paid-Up Participant and shall not be entitled to share further in any distribution under the Plan until all other Participants become Paid-Up Participants. Nothing in the Plan shall impose any duty on the directors of the New Company to inquire as to amounts so realized from sources other than the New Company; nor shall any director be liable, in the absence of bad faith, on account of any distribution or portion thereof made to anyone not entitled thereto. No Secured Participant shall be under any obligation to account to the New Company or to any other Participant or otherwise because the amounts paid to him and his predecessors in interest in accordance with the Plan, together with the *pro rata* share of amounts realized on the Collateral or other security securing the obligation to which his claim relates, are in excess of such claim.

(b) The Board of Directors of the New Company shall fix an appropriate Record Date with respect to each distribution.

(c) Distributions payable to Prudence Bond Participants and to Prudence Certificate Participants shall be

made (1) to Reserved Right Participants registered as such on the New Company's Register pursuant to subdivision (e) of this paragraph 3; (2) to Prudence Bond Participants and Prudence Certificate Participants, other than Reserved Right Participants and those referred to in subdivision (d) below, as follows:

(i) to the persons whose names are certified to the New Company by the custodian of the register of the particular issue or series, as the case may be, as the registered holders thereof (or of instruments representing beneficial interests therein, such as, but not necessarily limited to Trustees' certificates) at the close of business on the applicable Record Date, excluding bonds or certificates, if any, in respect of which distributions are to be made to Reserved Right Participants; such distributions to be made by checks drawn to the order of such persons and mailed to them at their addresses as certified by the custodian of the appropriate register, or delivered to them in person;

(ii) to the custodian of the sinking or retirement fund of the particular issue or series as the case may be, in respect of bonds or certificates certified by such custodian to have been purchased by such fund, excluding bonds or certificates, if any, in respect of which distributions are to be made to Reserved Right Participants; and

(iii) in the case of Prudence Bonds or Prudence Certificates as to which no such certification is given (excluding bonds or certificates, if any, in respect of which distributions are to be made to Reserved Right Participants), distributions shall be made to the persons presenting the same for notation of the making of such distributions.

The New Company shall be fully protected and discharged from all responsibility with respect to all distributions made as in this subdivision (c) provided.

(d) Distributions payable to Prudence Certificate Participants (other than Reserved Right Participants) in respect of guarantee claims on any issue of Prudence Certificates for which no register (other than the New Company's Register) is being maintained for the recordation of current transfers (such as, but not necessarily limited to, the so-called Hotel Taft and Langham issues) shall be made, in the first instance, to such persons as shall present such Certificates to the New Company for registration as provided below or as shall submit to the New Company proof satisfactory to it of their ownership of such Certificates. The New Company shall register as a Participant, in respect of the guarantee claim on any such Certificate, the person first presenting such Certificate or such proof as aforesaid, and thereafter distributions in respect of such claim shall be made to such Participant or his registered assignee as provided in the following subdivision (e). The New Company shall be fully protected and discharged from all responsibility with respect to all distributions made as in this subdivision (d) provided.

(e) The New Company shall keep a Register of the names and addresses of all Participants, except Prudence Bond Participants and Prudence Certificate Participants to whom distributions are to be made as provided in clause (2) of the foregoing subdivision (c) of this paragraph 3. The Section 77B Trustee shall prepare and deliver to the New Company a list, as of the Effective Date, of all Participants (except Prudence Bond Participants and Prudence Certificate Participants) showing, in the case of each such Participant, his name and address, and the nature and amount of his claim or claims; and such list shall constitute the New Company's Register as of the Effective Date. The New Company shall be protected in all respects in relying upon such list as correct as of the Effective Date.

Upon receipt by the New Company of an appropriate written assignment, duly executed and acknowledged by a person registered as a Participant in the New Company's Register and specifying the name and address of such assignee (or, in the New Company's discretion, upon receipt of such other evidence of assignment as shall be satisfactory to the New Company), the name and address of such Participant shall be stricken from the New Company's Register and the name and address of his assignee substituted. Unless and until the New Company shall have received a written assignment as aforesaid by a person registered as a Participant in the New Company's Register (or, if the New Company, in its discretion, shall consent to accept other evidence of assignment, unless and until the fact of such assignment shall have been recorded in the New Company's Register), the New Company shall not be affected by notice of any assignment by such person and shall be protected in all respects in treating such person as a Participant, notwithstanding such an assignment or the receipt of notice thereof by the New Company.

Distributions payable to Participants registered as such in the New Company's Register shall be made to such Participants of record at the close of business on the appropriate Record Date, by checks drawn to their order and mailed to them at their addresses as shown in the New Company's Register, or delivered to them in person. The New Company shall be fully protected and discharged from all responsibility with respect to all distributions made as in this subdivision (e) provided.

(f) The New Company, upon notice to the Participants affected, may deposit any amount distributable under the Plan in a bank or trust company which is a member of the New York Clearing House Association (or, if the New Company shall so elect, in the case of Prudence Bond Participants and Prudence Certificate Participants, with the custodian of the register of the particular issue or series) as a trust fund for the benefit of such Participants, with

appropriate instructions as to the disbursement of such amount, such action to fully protect the New Company and discharge it from all responsibility with respect to such distribution.

(g) The realization of the New Company's assets and the reduction thereof to cash to be made pursuant to this Article IV shall be completed, and all distributions under the Plan to Participants shall be made, within five years from the Effective Date; provided, however,

(1) that if so determined by vote of the Board of Directors (concurred in by directors of both classes) the New Company, at least one hundred and eighty days prior to the termination of such five-year period, may give notice to the Participants (by publication or otherwise in such manner as the Board of Directors by such vote may specify) that in the judgment of the New Company it would be in the interests of the Participants to continue the activities of the New Company, for the purposes of the Plan, for a further specified period not exceeding an additional five years (subject to earlier termination by majority vote of the whole Board of Directors); and

(2) that in case such notice is so given the New Company's activities shall be so continued (i) if prior to the expiration of ninety days from the giving of such notice, a majority in amount of the Participants shall not have filed written objection thereto, or (ii) in case affirmative approval of such continuation is legally required, then if such affirmative approval shall have been effectively given within such ninety-day period.

(h) The RFC's claim as a Participant shall be allowed in the amount of $11,347,775.50, without prejudice to such right as the RFC may have, under the provisions of Section 77B(c)(9), or other applicable provisions of law, to be compensated for services rendered and to be reimbursed for expenses incurred in connection with the proceedings and the Plan.

(i) Unless prior to the Effective Date his claim (1) shall have been expressly withdrawn, released or compromised, or (2) shall have been expunged by order of the Court, no action taken subsequent to February 1, 1935, by or on behalf of any holder of a guarantee claim against the Debtor with respect to his Collateral, shall bar any such claimant from participating in the benefits of the Plan to the extent herein provided.

ARTICLE V.

Valuation of Collateral and Other Security.

For the purposes of the distributions provided for in paragraph 2 of Article IV of the Plan, the Collateral or other security securing, on the Effective Date, the claim of any Secured Participant or the obligation to which such claim relates, shall be valued (in accordance with the limitations hereinafter in this Article V prescribed) at the reasonable value thereof as at the Effective Date by three salaried individual Appraisers to be employed by the New Company, each of whom shall be a real estate appraiser of recognized standing or a Professional Engineer within the meaning of Article 55 of the Education Law of the State of New York.

The Appraisers shall be selected in the manner hereinafter set forth and shall be controlled in the making of such valuations by the following limitations:

(a) In any case in which the Collateral or other security shall include a mortgage upon real estate, the value of the mortgage shall be deemed to be the New Loan Value of such real estate less the amount owing on any liens or encumbrances which are senior to the lien of such mortgage;

(b) In any case in which the Collateral or other security shall include real estate, the value of such real estate shall be deemed to be the New Loan Value of such real estate less the amount owing on any liens or encumbrances thereon;

(c) In determining the value of the bond secured by any mortgage or the value of any other obligation to be valued under the Plan, the Appraisers shall take into consideration the reasonable probability of collecting thereon under any then existing laws and the probable cost of effecting such collection, and shall estimate as nearly as practicable the net amount which might be reasonably realized therefrom.

The Appraisers shall in each case furnish a report to the New Company in the form of an affidavit of appraisal, which shall be deemed to be made in these proceedings, which shall set forth the pertinent facts and circumstances upon which the appraisal is based, including the appraised value of the real estate as of the Effective Date in every case where the Collateral or other security shall include or consist of real estate or a mortgage upon real estate. Whenever the appraised value of real estate is set forth in an affidavit there shall also be included a statement that in arriving at such valuation the Appraisers have taken into consideration, among other elements, the earnings of such real estate, the land value, the value of any improvements thereon, the replacement costs of such improvements, recent sales of real property, if any, in the vicinity, the assessed value of the property, the type of improvement and present demand for space of such a character, the adequacy of the improvement, depreciation, obsolescence, neighborhood trends, the general condition of the improvement, the cost of making necessary repairs and of modernization if any be required, the amount of real estate taxes to which the property is subject, the cost of operation, if a hotel the general character of its management, and all other factors which in the opinion of the Appraisers have a bearing upon such valuation.

The Appraisers shall act by a majority vote, but if no two of their opinions shall agree with respect to an appraisal or a New Loan Value, then (subject to the proviso hereinabove contained in the definition of New Loan Value) the appraisal or New Loan Value, as the case may

be, shall be the average of the amounts fixed therefor by each Appraiser.

All valuations (a) shall be made and submitted in writing to the Court within six months from the Effective Date unless the Court, for cause shown, shall extend such period; (b) shall be noticed to such creditors and in such manner (by publication, mail or otherwise) as the Court may determine; and (c) in the case of the valuation of each item, shall become final for all purposes of the Plan unless, within such time as the Court may fix, written objections to such valuation shall be filed with the Court by not less than 10% in amount of the Secured Participants secured by such item, or by the duly authorized trustee or other representative of such amount of Secured Participants, or by not less than 10% in amount of the Unsecured Participants. In the event of the filing of any such objection as aforesaid, the same shall be brought on for hearing before the Court by the New Company in accordance with such procedure as the Court shall specify, and the determination of the Court as to such objection shall be final, without appeal by any party to any court of appellate jurisdiction.

Each Appraiser shall serve for such salary as shall be specified by the Board of Directors of the New Company and shall be selected in the following manner: one by the majority vote of the Class A directors; one by the Class B directors; and one by the concurring vote of (a) a majority of the Class A directors, and (b) the two Class B directors. All three selections shall be made within fifteen days after the Effective Date and shall be submitted forthwith to the Court and be subject to its approval. If (i) the selection of an Appraiser shall not have been so made and submitted by the directors, or (ii) the Court shall have disapproved a selection and no substitute selection shall have been made by the directors within fifteen days after such disapproval, a vacancy shall be deemed to exist which shall be filled by designation of the Court from a panel of names of appraisers which the directors of the New Company, severally or jointly, shall submit to the Court.

In the event that any Appraiser shall resign, die or become incapable of acting, a successor shall be appointed in the same manner as provided for the appointment of his predecessor. The salaries of the Appraisers and all other expenses incidental to their work shall be paid by the New Company.

ARTICLE VI.

Acceptance of the Plan.

The Plan makes no separate provision for creditors who do not accept it, but treats both assenting and dissenting creditors alike. Accordingly the Plan shall not become operative or be confirmed by the Court unless duly accepted by or on behalf of creditors holding two-thirds in amount of the claims of each class whose claims have been allowed and would be affected by the Plan.

ARTICLE VII.

Tax Claims of the United States of America.*

The United States Collector of Internal Revenue has filed claims for income taxes in these proceedings against the Debtor. Such tax claims shall have the same priority and preference, if any, and the same remedies shall exist for their collection, as if the proceedings for the reorganization of the Debtor had not intervened. All statutes of limitation upon the collection of such tax claims shall be suspended during the time the proceedings for the reorganization of the Debtor are pending and, if such tax claims shall be adjudged to be a lien upon, or to be entitled to priority or preference with respect to, the assets of the Debtor, for such additional period of time as such claim or any part thereof remains unpaid. Subject to its approval the Court shall retain jurisdiction over the assets

* After the proposal of the Plan, such claims in respect of all taxable periods prior to January 1, 1937, were compromised pursuant to the Court's order of May 5, 1938, and payment in full has been made of the compromised claims. In addition, the Federal tax return for the calendar year 1937 has been audited and no tax found due.

of the Debtor (including the assets to be vested in the New Company pursuant to Article III hereof) and over all parties appearing in the proceedings for the reorganization of the Debtor for the purpose of carrying out and giving effect to any and all provisions of the Plan and the decree confirming the same, in so far as the Plan as so confirmed affects and applies to such tax claims.

ARTICLE VIII.

Expenses of the Proceedings and the Plan.

Payment shall be made, as provided in Article III hereof, of (1) the expenses of the proceedings and the Plan, as approved by the Court, including all costs of administration and other allowances made or to be made by the Court to such parties as the Court may deem entitled thereto under the provisions of Section 77B, and (2) all Federal taxes, if any, due from the Section 77B Trustee, in respect of the period between December 31, 1937 and the Effective Date, whether or not a claim for such taxes shall have been filed or allowed by the Court.

ARTICLE IX.

Execution of the Plan.

As soon as practicable after the confirmation of the Plan by final order of the Court, the Plan shall be consummated by the vesting in the New Company of the business and assets required to be so vested by the provisions of Article III hereof and the issuance of the entire authorized capital stock of the New Company as provided in such Article III. Such final order shall contain all appropriate provisions in aid of the consummation of the Plan and to compel all necessary parties to comply therewith and to make, execute and deliver any instruments necessary to such consummation. All proceedings to be taken and instruments to be executed in the consummation of the Plan, including, without limita-

tion, the certificate of incorporation and the by-laws of the New Company, shall be subject, in the discretion of the Court, to its approval.

ARTICLE X.

MISCELLANEOUS.

Subject to the provisions of Article V hereof, notices under the Plan to Participants and to other parties in interest, if any, may be given by publication once in each week for two successive weeks in a daily newspaper of general circulation in the City of New York.

The statements and figures contained in the Plan and in the Introductory Statement preceding the Plan have been derived from sources believed to be reliable, but none of them is to be construed as a warranty or representation.

In respect of any action taken to carry out any provision of the Plan and involving a legal question, the directors, officers, employees and agents of the New Company shall be protected, in the absence of a showing of bad faith, in relying upon the advice of its counsel.

No portion of any of the headings to the numbered Articles or paragraphs of the Plan nor any footnote therein shall be a part of the Plan or affect the meaning of any of the provisions thereof.

Dated, April 12, 1938.

RECONSTRUCTION FINANCE CORPORATION,
By JEROME THRALLS,
Special Representative.

The Hecla Press : : New York City

79

United States District Court

EASTERN DISTRICT OF NEW YORK.

IN THE MATTER OF THE PRUDENCE COMPANY, INC., Debtor.	In Consolidated Proceedings for Reorganization under Section 77B of the Bankruptcy Act,
In the Matter of the General Plan of Reorganization proposed by Reconstruction Finance Corporation.	Nos. 27496 and 27028.

This Court having heretofore entered an order, dated August 16, 1935, ordering, adjudging and decreeing as to the manner, among other things, in which claims and interests of creditors in this proceeding should be filed or evidenced for the purposes therein set forth, including participation in any plan of reorganization which might be confirmed herein; and

Reconstruction Finance Corporation (hereinafter called the RFC) having heretofore filed its petition, verified April 12, 1938, proposing a Plan of Reorganization for the Debtor herein, dated April 12, 1938 (hereinafter called the Plan), and this Court by order to show cause dated April 13, 1938, having directed that the parties and interveners herein and all other persons interested as creditors, stockholders, or otherwise, and the Section 77B Trustees of the Debtor, show cause at a term of this Court on April 21, 1938, why an order should not be made adjudging the Plan to have been duly proposed, classifying the creditors as therein set forth, adjudging the Plan to be fair, equitable, non-discriminatory and feasible and to comply with Section 77B of the Bankruptcy Act, and confirming the

Plan; and numerous sessions of the hearing on said petition and order to show cause having been had; and such hearing having been adjourned from time to time by written order of this Court or by orders made in open court; and

The RFC having heretofore proposed certain amendments to the Plan, under date of June 17, 1938, and July 22, 1938, respectively, and this Court, by order dated August 3, 1938, having adjudged, among other things, that the Plan, amended as so proposed by the RFC, was fair and equitable and did not discriminate unfairly in favor of any class of creditors or stockholders and was feasible; and

The RFC having filed its further petition, verified May 5, 1939 (hereinafter sometimes referred to as the Petition for Confirmation), and this Court, by order to show cause dated May 5, 1939, having duly directed that cause be shown at a term of this Court on May 19, 1939, why an order should not be made, as contemplated by the Petition for Confirmation, which shall, among other things, (a) provide how and to whom distributions shall be made under the amended Plan; (b) amend, to the extent required to give effect to such provisions, the previous orders of this Court herein, including the aforesaid order dated August 16, 1935; (c) approve all amendments proposed by the RFC to the Plan, including those proposed in the Petition for Confirmation; (d) confirm the Plan as amended; and (e) direct the Section 77B Trustee of the Debtor to vest forthwith in the New Company provided for in the amended Plan the assets and business thereby required to be so vested, free and clear, except as provided in the amended Plan, of all claims and interests of the Debtor, its stockholders and creditors, and others, and further, to transfer to such New Company, subject to all then existing equities and rights of third parties therein, all assets held by said Section 77B Trustee for the account of others; and why such other, further and different relief should not be granted in the premises as may be just and proper; and

A hearing on said petition and order to show cause dated May 5, 1939, having been had on May 19, 1939, and an adjourned session of such hearing having been had on May 26, 1939, and the RFC at such hearing and adjourned session having proposed certain further amendments to the amended Plan under date of May 19, 1939, and May 26, 1939, respectively; and

The Section 77B Trustee herein having submitted and filed in this proceeding his own affidavit and the affidavit of Ira K. Balsam, both dated May 19, 1939, and the supplemental affidavit of Ira K. Balsam, dated May 26, 1939, respecting claims allowed herein, and the requisite acceptance in writing of the amended Plan having been so filed, and due proof having been submitted as to the performance of all other conditions precedent to confirmation of the amended Plan;

Now, upon said order of August 16, 1935, and upon said petitions and orders to show cause, together with proof of due publication, service and mailing of notice thereof as therein provided, and upon the Plan, the aforesaid acceptance thereof, and all proceedings heretofore had herein, it is

ORDERED, ADJUDGED AND DECREED, and this Court does FIND, as follows:

1. By an order entered herein, dated April 22, 1938, this Court adjudged the Plan duly proposed.

2. By an order entered herein, dated April 25, 1938, this Court adjudged the Debtor to be insolvent. No class of stockholders of the Debtor is affected by the Plan and the Plan properly makes no provision for any such stockholders.

3. By an order entered herein, dated May 3, 1938, this Court directed (a) that any party in interest desiring to make objections to, or propose changes in or modifications of, the Plan, might file such objections or such proposed

changes or modifications in writing on or before May 27, 1938 (which time was thereafter extended); (b) that the hearing on the Plan be adjourned until June 10, 1938, at which time such objections or proposed changes or modifications should be considered; (c) that the Section 77B Trustees of the Debtor publish notice of the hearing of June 10, 1938, and of the opportunity to file such objections and proposals; and (d) that a copy of the Plan and an appropriate form of acceptance, together with a copy of such published notice, be mailed to creditors not later than May 13, 1938. Notice was published as directed, and copies of the Plan and of the published notice, and a form of acceptance, were duly mailed to creditors on or before May 13, 1938.

4. Objections to and proposed changes in and modifications of the Plan were filed herein, and were considered on June 10, 1938, and at adjourned sessions of the hearing on the Plan. Amendments to the Plan were offered by the RFC in proposals dated June 17, 1938, and July 22, 1938, respectively, and such proposals were considered at adjourned sessions of the hearing on the Plan. Copies of the RFC's proposed amendments were served on the parties and interveners herein prior to such adjourned sessions, and arguments of counsel thereon were heard. None of the RFC's amendments was or is materially adverse to the interest of any creditor other than the RFC.

5. By order of this Court dated August 3, 1938, it was adjudged (a) that the Plan, amended as proposed by the RFC as aforesaid, was fair and equitable and that it did not discriminate unfairly in favor of any class of creditors or stockholders and that it was feasible; (b) that the amended Plan complied with the provisions of subdivision (b) of Section 77B of the Bankruptcy Act; (c) that the Debtor was not a utility, and it was therefore unnecessary to comply with the provisions of subdivision (e), clause (2), of Section 77B; and (d) that for the purposes of the

amended Plan and its acceptance, creditors of the Debtor whose claims would be affected thereby should be classified as follows: (1) the United States of America; (2) creditors who came within the definition of Secured Participants as set out in Article 1 of the amended Plan; and (3) all other creditors whose claims would be affected by the amended Plan. The RFC is an Unsecured Participant as defined in the amended Plan.

6. In its Petition for Confirmation and at the hearing thereon held May 19, 1939, and at the adjourned session thereof held May 26, 1939, the RFC proposed further amendments to the amended Plan. None of such amendments is materially adverse to the interest of any creditor. Copies of this Court's order to show cause, dated May 5, 1939, issued in respect of such Petition, together with copies of all papers thereto annexed, were duly served, and notices in the form therein set forth were duly published and mailed, all as in said order provided.

7. All provisions of such proposed further amendments with respect to distributions under the amended Plan (including, but without limitation, the proposed further amendments of paragraphs 2 and 3 of Article IV) are hereby adopted by this Court with the same force and effect as though set forth in detail in this order; and all provisions (including, but without limitation, all provisions as to how claims and interests should be evidenced for the purpose of participating in any plan of reorganization in this proceeding) contained in the order of this Court dated August 16, 1935, or in any other order heretofore entered in this proceeding, are hereby amended to the extent required to give effect to the foregoing. The assignment, on or after February 1, 1935 and prior to the Effective Date of the amended Plan, of a bond or of a mortgage participation certificate issued by Prudence Bonds Corporation and guaranteed by the Debtor (or of an instrument representing a beneficial interest therein, such as,

but not necessarily limited to, a Trustee's certificate) shall be deemed, for all purposes of any plan of reorganization herein, to have effected an assignment of the assignor's guarantee claim against the Debtor (whether or not an instrument evidencing the assignment of such claim has been filed with the Section 77B Trustee) unless the assignor reserved to himself the rights against the Debtor based upon the Debtor's guarantee of such bond or certificate; provided, however, that unless such assignor, by proof filed with the Clerk of this Court on or before July 15, 1939, establishes to the satisfaction of this Court as evidenced by an adjudication, upon a hearing after such notice to the current holder of such bond or certificate and to the custodian of the register of the particular issue or series as this Court may direct, that such a reservation was made, it shall be conclusively presumed that no such reservation was made.

8. By its aforesaid order dated August 16, 1935, this Court decreed that for the purpose of accepting or consenting to any plan of reorganization, claims and interests should be evidenced by the filing and allowance thereof in the manner therein set forth. Paragraph 9 of said order provided among other things that duly filed claims should be deemed finally allowed unless objections were interposed prior to December 1, 1935. The time permitted for interposing such objections was thereafter variously extended, but it has now expired.

9. The aggregate amount of claims which have been allowed herein and remain unpaid is $133,723,298.95, consisting of the following, as more particularly set forth in the affidavits of Ira K. Balsam dated May 19, 1939, and May 26, 1939, respectively, hereinabove referred to:

(a) Claims in respect of the guarantee by the Debtor of bonds issued by Prudence-Bonds Corporation, in the principal amount of such bonds outstand-

ing as of February 1, 1935 (except such bonds as were owned by the Debtor at any time on or after February 1, 1935 and prior to said Effective Date), together with interest thereon due and unpaid as of February 1, 1935. The aggregate amount of such allowed claims is $58,833,179.79, consisting of $54,072,645.00 in respect of principal and $4,760,534.79 in respect of interest.

(b) Claims in respect of the guarantee by the Debtor of certificates issued by Prudence-Bonds Corporation, in the principal amount of such certificates outstanding as of February 1, 1935 (except such certificates as were owned by the Debtor at any time on or after February 1, 1935 and prior to said Effective Date) together with interest thereon due and unpaid as of February 1, 1935; provided, however, that all claims in respect of certificates of the so-called 1111 Park Avenue, Park Place Dodge, 100 West 55th Street, Blind Brook, Worthco and Dryden issues have been discharged by the payment thereof or by releases contained in the respective plans of reorganization of such certificate issues. The aggregate amount of such allowed claims is $50,857,852.86, consisting of $47,690,401.13 in respect of principal and $3,167,451.73 in respect of interest;

(c) Claims in respect of the guarantee by the Debtor of single mortgages (other than mortgages securing bonds or certificates issued by Prudence-Bonds Corporation) in the aggregate amount of $12,523,461.00;

(d) The RFC's claim, allowed for voting purposes in the aggregate amount of $11,357,577.45;

(e) Other claims in the aggregate amount of $151,227.85.

All claims and interests founded upon bonds or mortgage participation certificates issued by the Debtor have been

discharged by reason of separate reorganizations thereof consummated in this proceeding.

10. The provisions of Sections 198, 224 and 267 of Chapter X of the Bankruptcy Act, as amended by the Act of Congress of June 22, 1938, are deemed applicable to this proceeding.

11. All amendments proposed by the RFC as aforesaid are hereby approved and declared effective by this Court, and Exhibit A hereto attached constitutes the amended Plan.

12. The amended Plan has been accepted in writing, and such acceptance has been filed in this proceeding by or on behalf of creditors of the Debtor holding at least two-thirds in amount of the claims of each class of creditors whose claims have been allowed and would be affected by the Plan. Creditors of the Debtor as classified by the order of this Court, dated August 3, 1938, for the purposes of the amended Plan and its acceptance, and acceptances of the amended Plan by such creditors, are as follows:

	Allowed Claims	*Acceptances*	*%*
1. United States of America	$ 400,000.00	$ 400,000.00	100
2. Secured Participants.	$122,214,493.65	$85,352,494.45	69.8
3. Other.	$ 11,508,805.30	$11,359,187.24	98.7

No acceptance of the amended Plan by or on behalf of stockholders of the Debtor of any class is requisite.

13. There has been filed in these proceedings a statement, verified in a manner hereby approved, showing what contracts of the Debtor are executory in whole or in part and what unexpired leases have been rejected and surrendered.

14. By reason of the number of outstanding securities of the Debtor, or guaranteed by the Debtor, and the extent of the public dealing therein, it would be impractical to prepare a statement showing what, if any, claims and shares of stock have been purchased or transferred by those accepting the amended Plan after the commencement or in contemplation of this proceeding, and the circumstances of such purchase or transfer, and accordingly it is hereby directed that such a statement be not filed.

15. By an order dated April 21, 1939, this Court, among other things, approved a proposed certificate of incorporation of and by-laws for Prudence Realization Corporation, the New Company contemplated by the amended Plan. Pursuant to said order, the New Company was thereupon duly organized under the Stock Corporation Law of the State of New York, with a certificate of incorporation and by-laws in the form approved as aforesaid. By said order this Court found that the persons named as directors in such certificate of incorporation had been duly designated as such, pursuant to the applicable provisions of the amended Plan, that the identity, qualifications and affiliations of such persons had been fully disclosed, and that the appointment of such persons as such directors was equitable, compatible with the interests of the creditors and stockholders and consistent with public policy. At the instance of the directors, the identity, qualifications and affiliations of the persons who are to be officers of the New Company, upon consummation of the amended Plan, together with the aggregate compensation to be paid to the principal officers of the New Company during the first year following the Effective Date of the amended Plan, have been fully disclosed by an affidavit of the Section 77B Trustee dated May 25, 1939. The appointment of such persons to such offices is equitable, compatible with the interests of the creditors and stockholders and consistent with public policy, and such aggregate compensation is approved as fair and reasonable.

16. After hearing all objections which have been made to the amended Plan and its confirmation, this Court is satisfied that:

(a) the Plan and all amendments thereto approved by this Court have been duly proposed and considered at a hearing or hearings duly noticed for their consideration, all in conformity with subdivision (d) of Section 77B;

(b) all creditors and stockholders of the Debtor and all other interested persons have had a fair opportunity to make objections to the amended Plan and its confirmation and to be heard thereon;

(c) the amended Plan is fair and equitable and does not discriminate unfairly in favor of any class of creditors or stockholders, and is feasible;

(d) the amended Plan complies with, and has been accepted as required by, all applicable provisions of law;

(e) the provisions of subdivision (e), clause (2), of Section 77B are not applicable;

(f) all amounts to be paid by the Debtor or by any corporation or corporations acquiring the Debtor's assets, and all amounts to be paid to committees or reorganization managers, whether or not by the Debtor or any such corporation, for services or expenses incident to the reorganization, have been fully disclosed and are reasonable, or are to be subject to the approval of the judge in charge of the proceeding;

(g) the offer of the Plan and all amendments thereto approved by this Court, and the acceptance thereof, have been made in good faith and have not been made or procured by any means or promises forbidden by the Bankruptcy Act;

(h) the Debtor, and every other corporation issuing securities or acquiring property under the amended Plan, are authorized by their respective charters or by applicable State or Federal laws, upon confirmation of the amended Plan, to take all action necessary to carry out the amended Plan;

(i) the identity, qualifications and affiliations of the persons who are to be directors or officers of the New Company, upon consummation of the amended Plan, have been fully disclosed, and the appointment of such persons to such offices is equitable, compatible with the interests of the creditors and stockholders and consistent with public policy; and

(j) all other conditions precedent, if any, to the confirmation of the amended Plan under any applicable provision of law, have been complied with.

17. The amended Plan is hereby in all respects approved and finally confirmed.

18. The Section 77B Trustee of the Debtor is hereby directed, solely in consideration for the issuance to such Trustee acting on behalf of the Debtor of all the authorized capital stock of the New Company, forthwith (a) to execute and deliver to the New Company an assignment substantially in the form annexed as Exhibit C to the Petition for Confirmation, and (b) to deliver and surrender to the New Company possession of and control over the assets and business to which such assignment relates. The date of the execution by such Trustee of such assignment shall be the Effective Date of the amended Plan. The Debtor is hereby ordered to join in the execution of such assignment, and the New Company is hereby ordered to execute the acceptance and undertaking set forth at the foot thereof. All depositaries having funds on deposit credited to the Debtor's estate are hereby directed to trans-

fer such accounts to the New Company upon the written request of the Section 77B Trustee; the signature of the Clerk of this Court shall not be required to effect the transfer of such accounts.

As soon as practicable, the Section 77B Trustee shall execute and deliver to the New Company such further instruments of assignment, transfer, grant and conveyance (including, without limitation, deeds of real estate, assignments of mortgages, endorsements and powers of attorney) and shall effect such manual deliveries to the New Company, as the New Company reasonably may require to further assure the vesting in the New Company, as provided in Article III of the amended Plan, of the assets and business thereby required to be so vested; and the Debtor is hereby ordered to join in the execution of such instruments upon the request of the New Company.

Each bond and certificate issued by Prudence-Bonds Corporation and any other instrument included among such assets which was guaranteed by the Debtor shall be stamped, prior to delivery to the New Company, with a legend to the effect that such guarantee has been cancelled.

Forthwith upon the issuance by the New Company of its stock as hereinabove provided, the Section 77B Trustee shall assign and transfer one share of Class A stock to each of the five Class A directors and one share of Class B stock to each of the two Class B directors of the New Company, whereupon, as provided in Article III of the amended Plan, each such director shall enter into a written agreement substantially in the form approved by the aforesaid order of this Court dated April 21, 1939. The Debtor is hereby ordered to join in the execution of each such assignment and transfer.

19. The assets and business to be vested in the New Company shall be free and clear of all claims and interests of the Debtor, its stockholders and creditors, and

others, except the following which shall remain outstanding:

(a) claims for amounts due as taxes to the United States of America and the State of New York, and the items provided for in Article VIII of the amended Plan,

(b) finally allowed claims against the property of the Debtor in respect of which the Debtor is not personally liable, and

(c) finally allowed claims of the character which shall entitle the holders thereof to be deemed Participants as defined in Article I of the amended Plan.

There are no claims or interests having priority except the claims and items referred to in the foregoing subdivision (a).

The claims referred to in the foregoing subdivision (b) shall be payable only out of the property against which they are claims.

The claims and items referred to in the foregoing subdivisions (a) and (c) shall be paid by the New Company, but only as follows:

The claims and the items referred to in the foregoing subdivision (a) shall be paid in full in due course out of the New Company's assets. Such claims and items shall not constitute liens upon such assets, but shall have priority over all distributions to Participants under the amended Plan and over all liabilities incurred by the New Company; and the New Company shall be entitled to sell all or any part of such assets free and clear of any charge in respect of such claims and items.

The claims referred to in the foregoing subdivision (c) shall not constitute liens upon the New Company's assets, and the New Company shall be entitled to sell all or any part of such assets free and clear of any charge in respect of such claims; provided, however, that nothing herein con-

tained shall be deemed to affect the lien, if any, to which any part of such assets was subject, immediately prior to the vesting thereof in the New Company, in respect of any such claim. The claims referred to in such subdivision (c) shall be payable, without interest, only as provided in Article IV of the amended Plan and only to the extent that the New Company's assets shall be sufficient to pay them, after reserving from such assets $70 for the New Company's capital and $70 for its surplus, and after payment of or provision for (i) the amounts and items referred to in the foregoing subdivision (a), and (ii) such liabilities as may be incurred by the New Company. Such surplus shall be available to pay for stock which may be purchased by the New Company under the options provided for in Article III of the amended Plan.

20. The Section 77B Trustee of the Debtor is hereby further directed to transfer to the New Company forthwith, subject to all then existing equities and rights of third parties therein, all assets held by said Section 77B Trustee for the account of others, or held by said Section 77B Trustee in any agency or other segregated account pending settlement or determination of equities or rights asserted by others. The moneys in the bank accounts denominated "The Estate of The Prudence Company, Inc., Debtor, Nos. 27496 & 27028, Servicing Fees Reserve Account", in Brooklyn Trust Company, 177 Montague Street, Brooklyn, N. Y., Kings County Trust Company, 372 Fulton Street, Brooklyn, N. Y., Lawyers Trust Company, 185 Montague Street, Brooklyn, N. Y. and The National City Bank of New York, Court Street at Montague Street, Brooklyn, N. Y., may be dealt with by the New Company, without further order of this Court, upon due settlement or determination of the New Company's interest therein, provided, however, that, pending such settlement or determination, the moneys in such accounts shall be retained in a segregated agency account or accounts; and the order

of this Court dated August 16, 1935, under which such moneys have heretofore been held by the Section 77B Trustee, and the order of this Court dated February 1, 1935, as amended by said order of August 16, 1935, are hereby amended to the extent required to give effect to the foregoing. Upon receipt of a certified copy of this order, the banks named herein shall take such steps as may be necessary or appropriate to effectuate the transfer of such accounts to the New Company.

21. The New Company is hereby directed to pay in full in due course all Federal taxes, if any, due from the Section 77B Trustee, in respect of the period between December 31, 1937 and the Effective Date of the amended Plan, whether or not a claim for such taxes shall have been filed or allowed by this Court.

22. On and after the Effective Date, the RFC's claim shall stand allowed in the amount of $11,347,775.50, without prejudice to such right as the RFC may have, under the provisions of Section 77B(c)(9), or other applicable provisions of law, to be compensated for services rendered and to be reimbursed for expenses incurred in connection with the proceedings and the amended Plan.

23. All causes of action or rights against present or former officers or directors of the Debtor, and against other parties arising out of or relating to the transactions giving rise to such causes of action or rights, including those asserted in the suits instituted in the Supreme Court of the State of New York, County of New York, by the Section 77B Trustees, captioned Stephen Callaghan, et al., Plaintiffs v. Frank Bailey, et al., Defendants, and by Julia Regan, et al., captioned Julia Regan, et al., Plaintiffs v. The Prudence Company, Inc., et al., Defendants, shall survive the confirmation and consummation of the amended Plan and shall not be deemed to have been abandoned.

24. The provisions of the amended Plan and of this order shall be binding upon (a) the Debtor, (b) all stockholders of the Debtor, (c) all creditors of the Debtor, secured or unsecured, whether or not affected by the amended Plan, and whether or not their claims or interests shall have been filed and, if filed, whether or not scheduled, allowed or allowable, including creditors who have not, as well as those who have, accepted the amended Plan, and (d) the New Company.

25. THIS COURT RESERVES JURISDICTION:

(a) to take all such further action as may be required in aid of the consummation of the amended Plan, including, but not limited to, the giving of such directions, authorizations or approvals as this Court may determine in regard to instruments of transfer and conveyance of the property dealt with by the amended Plan; and to take all action contemplated by the provisions of Article V of the amended Plan to be taken by this Court with respect to the valuations therein provided for;

(b) To approve duly proposed changes in and modifications of the amended Plan, after hearing duly noticed, subject to the right of any creditor who shall previously have accepted the amended Plan to withdraw his acceptance, within a period to be fixed by the judge in charge of the proceeding and after such notice as such judge may direct, if, in the opinion of such judge, the change or modification will be materially adverse to the interest of such creditor; provided, however, that the amended Plan as changed or modified shall comply with all applicable provisions of law and shall have been or shall thereafter be duly accepted;

(c) from time to time to make such orders, adjudications and decrees respecting claims or the assignment or registration thereof or distributions thereon,

including, without limitation, adjudications of the character contemplated by paragraph 7 hereof, and respecting the assets, equities and rights referred to in paragraph 20 hereof, all as justice may require;

(d) to allow and direct the payment of all expenses, costs and allowances provided for in Article VIII of the amended Plan;

(e) upon the termination of the proceeding, to enter a final decree discharging Stephen Callaghan, John M. McGrath and William T. Cowin as Trustees of the Debtor's estate (the first two named having heretofore resigned), making such provisions as may be equitable, by way of injunction or otherwise, and closing the case; to discharge the Debtor from its debts and liabilities, and to terminate and end all rights and interests of its stockholders, except as provided in the amended Plan; and

(f) generally to determine any and all matters pertaining to this proceeding or to the amended Plan and not determined heretofore or by this order.

26. The Section 77B Trustee is directed to publish, on or before June 3, 1939, in the New York Times and Brooklyn Daily Eagle, newspapers of general circulation in the City of New York, a notice of the entry of this order in substantially the following form:

In the United States District Court, for the Eastern District of New York; In the Matter of The Prudence Company, Inc., Debtor; consolidated proceedings for the reorganization of a corporation under Section 77B of the National Bankruptcy Act, Index Nos. 27496 and 27028;

To all creditors and stockholders of The Prudence Company, Inc., and all other persons in any wise interested in the above entitled proceeding;

Take notice that an order dated May 26, 1939, has been entered herein which, among other things, (a) provides how and to whom distributions shall be made under the general Plan of Reorganization of the said Debtor, dated April 12,

1938, proposed by Reconstruction Finance Corporation, including a provision (more fully set forth in the amended Plan) to the effect, in the case of each claim founded on the Debtor's guarantee of a bond or certificate, that such distributions shall be made to the holder of such bond or certificate unless a person who disposed of such bond or certificate between February 1, 1935 and the Effective Date of the amended Plan, by proof filed with the Clerk of this Court on or before July 15, 1939, establishes to the satisfaction of the Court that he reserved to himself the rights against the Debtor based on the Debtor's guarantee thereof, in which case such distributions shall be made to such person; (b) amends, to the extent required to give effect to such provisions, the previous orders of the Court herein, including the order dated August 16, 1935, relative, among other things, to the manner in which claims and interests of creditors in this proceeding should be filed or evidenced for the purposes therein set forth; (c) approves all amendments proposed by Reconstruction Finance Corporation to said Plan, including those proposed by it in its petition dated May 5, 1939, and at the hearing thereon and the adjourned session thereof; (d) confirms the Plan as amended; and (e) directs the Section 77B Trustee of the Debtor to vest forthwith in the New Company provided for in the amended Plan the assets and business thereby required to be so vested, free and clear, except as provided in the amended Plan, of all claims and interests of the Debtor, its stockholders and creditors, and others, and further, to transfer to such New Company, subject to all then existing equities and rights of third parties therein, all assets held by said Section 77B Trustee for the account of others, or held by said Section 77B Trustee in any agency or other segregated account pending settlement or determination of equities or rights asserted by others.

Copies of said order and copies of the amended Plan as confirmed by the Court may be obtained upon request at the office of the Section 77B Trustee of the Debtor, 331 Madison Avenue, New York, N. Y., or at the office of the solicitors for Reconstruction Finance Corporation, Messrs. Root, Clark, Buckner & Ballantine, 31 Nassau Street, New York, N. Y.

WILLIAM T. COWIN,
Section 77B Trustee of The Prudence Company, Inc.

and the Section 77B Trustee is further directed to mail, on or before June 3, 1939, a copy of said notice to all persons who have duly filed proofs of claim herein (or their

assignees on the records of such Trustee) unless such claims have been heretofore discharged or disposed of otherwise than by their allowance. The cost of such publication and mailing shall be paid out of the funds in the Debtor's estate, and promptly upon completion thereof due proof of such publication and mailing shall be filed with the Clerk of this Court by the Section 77B Trustee. No failure to comply with the provisions of this paragraph 26 shall in any wise affect the effectiveness of the other provisions of this order or of the amended Plan.

27. The hearing on the above mentioned petition of April 12, 1938, the order to show cause dated April 13, 1938, the amended Plan, the Petition for Confirmation, and the order to show cause dated May 5, 1939, is hereby adjourned to June 23, 1939.

Dated, May 26, 1939.

GROVER M. MOSCOWITZ,
U. S. D. J.

[fol. 36] IN UNITED STATES DISTRICT COURT, EASTERN DISTRICT OF NEW YORK

[Same title]

REPLYING AFFIDAVIT OF A. JOSEPH GEIST, READ IN SUPPORT OF MOTION

STATE & CITY OF NEW YORK,
County of New York, ss:

A. Joseph Geist, being duly sworn, deposes and says: That he is the Trustee of Zo-Gale First Mortgage Participation Certificate Issue, and submits this affidavit in reply to the answering affidavit interposed by William T. Cowin in opposition to the application made by your deponent for an order determining that the interests of the Prudence Realization Corporation in the Zo-Gale Issue are subordinate to the certificates held by the general public.

Your deponent respectfully calls the attention of this Court to certain pertinent facts and data which, in your deponent's opinion, constitute the basis for the determination of the question involved in this proceeding. Your deponent has annexed to the petition in support of the order sought herein a copy of the certificates issued in the Zo-Gale Issue by Prudence-Bonds Corporation and which were sold and guaranteed by The Prudence Company, Inc. to the general public. The certificate provides in part thereof as follows:

"Prudence-Bonds Corporation, hereinafter called 'The Corporation', has received from —— for the purchase of, and hereby assigns to the purchaser, an undivided share equal to that amount, with interest thereon at the rate of —%, —— for $—— dated —— —, 19—, due —— —, 19—, and in the first mortgage securing the same, covering ——."

[fol. 37] The certificate, which was issued by Prudence-Bonds Corporation and guaranteed and sold by The Prudence Company, Inc., which is therein referred to as the "Guarantor", provides in part thereof as follows:

"2. The Corporation upon the receipt of the interest and principal of said bond and mortgage shall distribute the same pro rata among the parties entitled thereto.

3. The Corporation and/or the Guarantor shall have full power to take any action it may deem necessary or desirable in order to enforce any of the provisions of said bond and mortgage and to protect the mortgage security.

4. The Corporation may for its own corporate account, be the holder or pledgee of similar shares in said bond and mortgage."

These extracts from the certificate issued by Prudence-Bonds Corporation brings sharply to light the position of The Prudence Company, Inc., the guarantor and seller of the certificates. It discloses that The Prudence Company, Inc. recognized that as a guarantor, debtor, it could not be the holder or pledgee of certificates issued in the series on a parity with those issued to the general public. It failed to reserve to itself the right to hold shares or retain shares for its own account.

The Prudence Realization Corporation, the successor in interest of The Prudence Company, Inc., cannot now seek to acquire greater rights than The Prudence Company, Inc. had, and cannot seek to establish that any interest retained by The Prudence Company, Inc., in the uncertificated issues is on a parity with the certificates held by the general public. The guarantee executed by The Prudence Company, Inc. places it squarely in the position of a debtor as to each person who holds a mortgage participation cer- [fol. 38] tificate and the equitable rule existing between debtors and creditors must be recognized and applied; to attempt to place the re-purchased and uncertificated portions of this mortgage held by The Prudence Company, Inc., the guarantor, on a parity with those sold and delivered to the certificate holders, would utterly and completely destroy this well-established and long existing rule of law.

No creditor without cause may be compelled to release a part or portion of the security to which he may look to satisfy the obligation due him, nor may the debtor while insolvent and unable to meet its obligation divert the security which was made expressly responsible for the payment of this existing obligation. Surely this principle is not subject to question. We must merely ascertain the facts, the origin and history of the certificates in question, the ownership of the certificates and from whom present holders acquired title, and apply the rules of law applicable to the facts found.

General History of Certificates Held by The Prudence Company, Inc. and of the Certificates Sold by it to the General Public

The Trustees of The Prudence Company, Inc., upon their appointment and qualification following the filing and approval of the plan of reorganization of The Prudence Company, Inc., debtor, came into the possession of certain assets including the unissued certificates and the re-purchased certificates involved herein.

The Prudence Company, Inc., a banking corporation, was engaged in the sale of guaranteed mortgage certificates to the general public. Its practice generally was to lend its money to owners of real estate on improved property, who would execute and deliver a bond and mortgage as security therefor. The Prudence Company, Inc. would then assign this bond and mortgage to Prudence-Bonds Corporation, and Prudence-Bonds Corporation would issue [fol. 39] undivided shares to The Prudence Company, Inc. These shares or certificates were thereupon guaranteed by The Prudence Company, Inc. and sold by The Prudence Company, Inc. to the general public.

The assignment of the bond and mortgage to Prudence-Bonds Corporation was in form absolute. However, your deponent has been informed and verily believes that Prudence-Bonds Corporation, the alter-ego of The Prudence Company, Inc., did not part with any consideration upon the assignment to it of the Zo-Gale bond and mortgage. Prudence-Bonds Corporation was a mere conduit used by The Prudence Company, Inc. for the issuance of the securities which were guaranteed and sold by The Prudence Company, Inc. to the general public.

Prudence-Bonds Corporation did not have the capital or financial resources to enable it to purchase the bond and mortgage assigned to it. The real purpose of the assignment of the bond and mortgage to Prudence-Bonds Corporation was fully carried out when Prudence-Bonds Corporation certified and delivered the certificates or shares in such bond and mortgage to The Prudence Company, Inc., so that the sale thereof by The Prudence Company, Inc. to the general public could be facilitated. That is the only way in which the Prudence-Bonds Corporation became involved in the transaction. In fact, the common stock of The Prudence Company, Inc. and the common

stock of Prudence-Bonds Corporation were both wholly owned and held by a common parent company, New York Investors Inc.

In the normal course of events, Prudence Company, Inc. sold to the general public certificates or undivided shares of the Zo-Gale issue, herein described, aggregating $382,800., leaving $7,200. worth of certificates unissued and in the portfolio of The Prudence Company, Inc. The proceeds that were received upon the sale of these certificates constituted the absolute property of The Prudence Company, [fol. 40] Inc. and at no time were considered or treated as the property of Prudence-Bonds Corporation.

In 1932, the Prudence Company, Inc. re-purchased two certificates, one in the sum of $500., and one in the sum of $300., which had theretofore been sold to the public, and had the certificates issued in its own name. As a result of various cancellations, The Prudence Company, Inc. also became entitled to a certificate for $16.67. The Prudence Company, Inc. in this manner re-acquired certificates totalling $816.67 additional.

William T. Cowin, president of Prudence Realization Corporation, the respondent herein, formerly a trustee of the debtor, states in his affidavit that in many instances The Prudence Company, Inc. re-acquired certificates theretofore sold to and held by the public, and that it was the intention of The Prudence Company, Inc. to hold such certificates in its own investment portfolio as an investment.

Your deponent does not take any exception to such statement, but respectfully submits that this presents an incomplete picture. The mortgagor, Zo-Gale Realty Co., Inc., undoubtedly paid interest on the whole mortgage. Who received the balance above that required to be paid to the certificate holders? Who received the interest on the unissued certificates of $7,200.?

Your deponent has been informed and verily believes that these interest payments were retained by The Prudence Company, Inc., who as the owner thereof, was entitled to receive such interest. The arrangement that existed was one of convenience only between The Prudence Company, and Prudence-Bonds Corporation, and it was acknowledged that The Prudence Company, Inc. at all times was the owner of the uncertificated portion of the mortgage.

The records show that The Prudence Company, Inc. at all times claimed ownership of the unissued portion of the Zo-Gale mortgage of $7,200 and this claim was recognized by the court. In the proceeding for the reorganization of [fol. 41] The Prudence Company, Inc., the Trustees on December 15th, 1937, procured an order to show cause why a certain proposed compromise of the claims asserted on behalf of The Prudence Company, Inc. in the reorganization of the Prudence-Bonds Corporation should not be accepted. The petition submitted in support of the compromise alleged certain claims arising out of eighteen series of bonds, and in addition asserted ownership of, "unissued certificates", that is, the difference between the face amount of the mortgage and the amount of certificates actually issued and sold to the public.

Annexed to that petition is a statement which sets forth the various proofs of claim filed in that reorganization proceeding on behalf of The Prudence Company, Inc. and the proposed compromise. The following is an extract in part:

"(1) We will accept subordination of the Prudence-Bonds of the eighteen series owned and held by us as Trustees of The Prudence Company, Inc. * * * as subordination is defined in paragraph 11 of the several plans of reorganization for the eighteen series of bond issues and also as provided for and defined in the order of Hon. Robert A. Inch made on July 21, 1937. We will submit our bonds for stamping with an appropriate legend indicating such subordination.

* * * * * * *

(3) We will withdraw and consent to the expunging of all the following proofs of claim heretofore filed by or on behalf of The Prudence Company, Inc. in the proceedings for the reorganization of Prudence-Bonds Corporation * * *"

These specific proofs of claim are then listed and the proposal continues:

"except in so far as any of the foregoing proofs of claim may constitute a claim in and to the uncertificated portions of certain certificated mortgages more fully described hereafter. * * *"

[fol. 42] The compromise was approved by this Court and the Trustees of The Prudence Company, Inc. received the uncertificated portion of the Zo-Gale certificate issue of $7,200. The approval by the Court of the proposal was an affirmation of the recognized existing fact that The Prudence Company, Inc. was at all times the true and equitable owner of the unissued portion of this mortgage, title to which was at all times claimed and asserted by The Prudence Company, Inc.

In point of fact, the affidavit submitted in opposition to the instant application seeks to capitalize that which it chooses to classify as the election of certificate holders, by virtue of the proofs of claim filed in the reorganization of The Prudence Company, Inc., to come in as unsecured creditors rather than as secured creditors, and by virtue of such election the unissued portion of this mortgage acquired a sanctimonious halo, and should now be declared to be on a parity with the certificates held by the public.

Your deponent has been informed and verily believes that in the proceeding for the reorganization of The Prudence Company, Inc. forms for filing proofs of claim were prepared and sent to all certificate holders by the Prudence Company, Inc. or the Trustees of The Prudence Company, Inc. A copy of the form of proof of claim which the certificate holder was requested to complete is annexed to the answering affidavit. The certificate holder, among other questions, was asked to list the security, that is, the certificates held by him in each issue and each certificate holder set forth the certificates held by him. The certificate holders thus filed proofs of claim as secured creditors.

The certificate holders are now sought to be charged with negligence in not having filed a proof of claim against the unissued certificates owned by The Prudence Company, Inc., and that they thereby released their right to assert a claim against these specific holdings of The Prudence Company, Inc. The proof of claim required the certificate [fol. 43] holders to state on such proof of claim those certificates which the certificate holder, "was on * * * February 1st 1935, * * * and still is, the lawful owner and holder of * * * participation certificate(s)".

We quote from paragraph 3 of the form of proof of claim:

"3. That the claimant was on February 1, 1935, the date of the approval of the petitions for the reorganization of

the Debtor herein, and still is, the lawful owner and holder of Prudence-Bonds Corporation mortgage participation certificate(s), and, if the same be not registered, of the coupons appurtenant thereto, which mortgage participation certificate(s) are described as follows:

Serial Number	Interest Rate	Principal Amount	Name of Issue
*	*	*	*

that the foregoing constitutes a statement of claimant's claim herein * * *."

The language employed was that of the debtor which prepared the proof of claim and not that of the certificate holder and, of course, must be construed strictly in favor of the certificate holders and against the debtor, The Prudence Company, Inc., which prepared the same.

This statement is not intended to be a concession that by filing such proof of claim the certificate holders waived their rights with respect to that portion of the certificates held by The Prudence Company, Inc., and did not constitute a release. In fact, we contend that the certificate holders' claims were originally filed as secured claims. The order of this court entered on February 19th, 1938, set forth in paragraph "12th" of the petition dated May 7th, 1940, recognizes the fact that a dispute existed as to said certificates held by The Prudence Company, Inc., or [fol. 44] the Trustees of The Prudence Company, Inc., and reserved for future determination the claim of The Prudence Company, Inc., that such certificates were in fact on a parity. The reservation of this question precludes the Prudence Realization Corporation, the successor of The Prudence Company, Inc., debtor, from making any greater claim than the Trustees of The Prudence Company, Inc., had to such uncertificated portion of such mortgage.

The reorganization of the Zo-Gale Issue expressly reserved to the certificate holders all their rights against The Prudence Company, Inc. (see paragraph #13 of the petition dated May 7th, 1940), which sets forth an excerpt from the original plan of reorganization, as amended by the order dated December 10th, 1937.

Your deponent disputes the contention urged by the respondent that if the certificates were held by the Prudence-Bonds Corporation, that they would be entitled to be placed on a parity with those held by the general public. This contention assumes a state of facts, which never existed, and could not possibly exist since Prudence-Bonds Corporation at no time paid any consideration for the bond and mortgage assigned to it and it was obligated under its understanding to issue Prudence Bonds in exchange therefor of the face amount of the mortgage assigned to it.

If Prudence-Bonds Corporation had purchased the certificates, then since no relationship of debtor and creditor existed or could exist between Prudence-Bonds Corporation and the general public, and since the certificates issued to the general public contained the express proviso that "The Corporation", Prudence-Bonds Corporation, might be the holder or pledgee of similar certificates for its own account, Prudence-Bonds Corporation in such circumstances would be entitled to have those certificates held by it declared to be on a parity with those held by the general public. The facts herein, however, estop the respondent from urging the position it seeks to adopt.

[fol. 45] The Prudence Company, Inc., in the reorganization of the Prudence-Bonds Corporation, litigated the question as to the parity of the bonds held by it with those held by the general public, and as stated in the affidavit of William T. Cowin, both the Special Master to whom this question was referred and the District Court determined that question adversely to the Trustees of The Prudence Company, Inc. The decision of that court is stare decisis in this proceeding.

Wherefore, your deponent respectfully prays that an order be made and entered herein declaring that the certificates held by the Prudence Realization Corporation in the sum of $816.67 and the unissued principal amount of the mortgage in the sum of $7,200 not represented by outstanding certificates, are subordinate to the certificates guaranteed by The Prudence Company, Inc., held by the general public.

A. Joseph Geist.

(Sworn to October 23, 1940.)

[fol. 46] IN UNITED STATES DISTRICT COURT, EASTERN DISTRICT OF NEW YORK

[Same Title]

Geist & Neter, Attorneys for Trustee; Morris A. Marks, of Counsel.

Irving L. Schanzer, Attorney for Prudence Realization Corporation, Respondent.

OPINION OF MOSCOWITZ, D. J.

MOSCOWITZ, D. J.

This is a petition to declare certain interests of the Prudence Realization Corporation in a bond and mortgage of the Zo-Gale Realty Co., Inc., to be subordinate to the interests of third party certificate holders. The Prudence Company, Inc., hereinafter referred to as "Prudence", had loaned money to Zo-Gale Realty Co., Inc., and received therefor the latter's bond and mortgage. These in turn were assigned by Prudence to Prudence Bonds Corporation, hereinafter referred to as "Prudence Bonds", the only consideration being the issue by Prudence Bonds to Prudence of certificates of interest in the bond and mortgage thus assigned. Prudence then sold the certificates to the public accompanied by its guaranty. The practice followed in these issues by Prudence and Prudence Bonds, both of which were controlled by the same interests, is well described in In re The Westover, 82 F. (2d) 177 (C. C. A. 2d), In re Prudence Co., Inc., 89 F. (2d) 689 (C. C. A. 2d), and In re Prudence Co., Inc., 98 F. (2d) 559 (C. C. A. 2d). As pointed out in In re Prudence Bonds Corporation, 79 F. (2d) 212 (C. C. A. 2d), Prudence Bonds assumed no liability with respect to the certificates.

Some of the certificates sold by Prudence to the public were subsequently repurchased by it. In connection with [fol. 47] the reorganizations of Prudence and Prudence Bonds, the latter released to the former, as part of a compromise, all interest which it had in the uncertificated portion of the Zo-Gale mortgage. It is these two interests in the Zo-Gale mortgage, both now in the hands of Prudence Realization Corporation, as successor to the Trustees of

Prudence, which the present petition seeks to have subordinated to the certificates in the hands of the public.

So far as the uncertificated portion of the mortgage is concerned, the controlling authorities support the proposition that where a debtor who guarantees mortgage certificates, also holds an interest in the mortgage, it cannot share in the collateral until certificate holders are paid, unless there is clear reservation in the certificate of the right to share on a parity. Pink v. Thomas, 282 N. Y. 10; Matter of Title & Mortgage Guaranty Co., 275 N. Y. 347. The respondent does not dispute this proposition but contends that it is inapplicable by reason of the fact that the uncertificated interest was allegedly obtained in connection with reorganization proceedings, and that accordingly parity is to be granted. The respondent having thus assumed parity as a result of the reorganization transaction, concludes that the parity so assumed is binding in this proceeding. Cf. Stoll v. Gottlieb, 305 U. S. 165.

The difficulty with the respondent's analysis rests in the assumption that its uncertificated interest was derived from the reorganization compromise and that the compromise agreement implied parity. Actually, however, the uncertificated interest of the respondent was not wholly derived in that manner. It should be remembered that the assignment of mortgage from Prudence to Prudence Bonds was without consideration, and that therefore, to the extent that mortgage certificates were not delivered by Prudence Bonds to Prudence, the real ownership, as between the parties, remained in Prudence. When, therefore, in connection with [fol. 48] the reorganization compromise, Prudence Bonds released to Prudence any interest it might have in the uncertificated portion of the mortgage, that release did not effect the transfer to Prudence of any substantial interest that it did not already have as against Prudence Bonds. Accordingly, there is no basis for disregarding the rule set forth in Pink v. Thomas, supra.

The facts of Pink v. Thomas, supra, also concerned a certificated interest and as to this also the Court refused to allow parity. This Court sees no reason for departing from that rule. No claim of waiver can properly be asserted by the respondent since this question of parity has at all times been reserved.

No reservation of parity for the guarantor, Prudence, having been inserted in the mortgage certificates, both the

certificated and uncertificated interests of the respondent, Prudence Realization Corporation are subordinate to certificates in the hands of the public.

Settle order on notice.

Grover M. Moscowitz, U. S. D. J.

January 25, 1941.

[fol. 49] IN UNITED STATES DISTRICT COURT, EASTERN DISTRICT OF NEW YORK

[Same title]

ORDER APPEALED FROM

A. Joseph Geist, as trustee, having moved this Court by order to show cause dated the 13th day of May, 1940, why an order should not be made and entered declaring that the interest of the Prudence Realization Corporation in and to the outstanding certificates in the sum of $816.67 and in and to the unissued certificates in the principal amount of $7,200 of the Zo-Gale Realty Co. Issue is subject and subordinate to the certificates issued by Prudence-Bonds Corporation, guaranteed by The Prudence Company, Inc., and held by the general public, and why payments of principal and interest on the certificates issued and unissued held by the Prudence Realization Corporation should not be deferred until the certificate holders have been paid in full the principal and interest guaranteed them under their certificates, and for such other and further relief as to the Court may seem just and proper in the premises, and the same having duly come on for hearing before the undersigned,

Now, upon reading and filing the order to show cause herein dated the 13th day of May, 1940, the affidavit of A. Joseph Geist, duly verified the 7th day of May, 1940, Exhibits 1 and 2 annexed thereto, the affidavit of William T. Cowin, duly sworn to the 26th day of September, 1940, Exhibits A, B, C and D annexed thereto, the reply affidavit of A. Joseph Geist, duly sworn to the 23rd day of October, 1940, and due deliberation having been had thereon, and after hearing Geist & Netter, by Morris A. Marks, Esq., attorneys for the trustee, in support of said motion, and [fol. 50] Irving L. Schanzer, Esq., attorney for the Prudence Realization Corporation, in opposition thereto, and upon

the opinion of this Court dated the 25th day of January, 1941, it is

Ordered, adjudged and decreed that the said motion be and the same is hereby in all respects granted; and it is further

Ordered, adjudged and decreed, that the interest of the Prudence Realization Corporation, successor in interest of The Prudence Company, Inc., in and to the certificates, issued and unissued, in the Zo-Gale Realty Co. Issue, be and the same is declared to be subordinate to the interest of third party certificate holders, and that the Prudence Realization Corporation, its successors and assigns, are not entitled to any distribution of interest or principal out of the trust estate on account of the certificates held by it until the third party certificate holders have been paid in full the principal and interest guaranteed under the certificates held by such third party certificate holder.

Dated, Brooklyn, New York, January 30th, 1941.

Grover M. Moscowitz, U. S. D. J.

[fol. 51] IN UNITED STATES DISTRICT COURT, EASTERN DISTRICT OF NEW YORK

[Same title]

NOTICE OF APPEAL

SIRS:

Please take notice that Prudence Realization Corporation, the respondent herein, hereby appeals to the United States Circuit Court of Appeals for the Second Circuit, both on the law and the facts, from an order made and entered in the above entitled proceeding on the 30th day of January, 1941, by Hon. Grover M. Moscowitz, and that said Prudence Realization Corporation hereby appeals from each and every part of said order as well as from the whole thereof.

Dated: New York City, New York, February 13th 1941.

Irving L. Schanzer, Attorney for Prudence Realization Corporation.

To: The Honorable Clerk of the United States District Court for the Eastern District of New York. Geist & Netter, Esqs., Attorneys for A. Joseph Geist, Trustee.

[fol. 52] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

[Title omitted]

STIPULATION DISPENSING WITH PRINTING OF PART OF RECORD

It is hereby stipulated and agreed by and between the attorneys for the respective parties to this appeal, that Prudence Realization Corporation, the appellant herein, may submit to the Court three copies of Exhibits "A", "B", "C", and "D" attached to the answering affidavit of William T. Cowin, dated September 26, 1940, in lieu of printing [fol. 53] each of said exhibits as part of the Record on this appeal from an order of Hon. Grover M. Moscowitz, United States District Judge, dated January 30, 1941.

Dated: New York, N. Y., February 11, 1941.

Irving L. Schanzer, Attorney for Prudence Realization Corporation. Geist & Netter, Attorneys for A. Joseph Geist, Trustee.

Feb. 18, 1941.

So ordered: August N. Hand, U. S. C. J.

[fol. 54] IN UNITED STATES DISTRICT COURT, EASTERN DISTRICT OF NEW YORK

[Title omitted]

STIPULATION AS TO RECORD

It is hereby stipulated and agreed that the foregoing is a true and correct transcript of the record of the said District Court in the above-entitled cause, as agreed on by the parties.

Dated, New York, March 11th, 1941.

Irving L. Schanzer, Attorney for Appellant. Geist & Netter, Attorneys for Appellee.

[fols. 55-56] Clerk's Certificate to foregoing transcript omitted in printing.

Opinion of Circuit Court of Appeals.

UNITED STATES CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 343—October Term, 1940.

(Argued June 9, 1941 Decided August 11, 1941.)

A. JOSEPH GEIST, Trustee,
Petitioner-Appellee,

— *v.* —

PRUDENCE REALIZATION CORPORATION,
Respondent-Appellant.

Appeal from the District Court of the United States for the Eastern District of New York.

In consolidated proceedings for the reorganization under Bankruptcy Act, §77B, of The Prudence Company, Inc., and Amalgamated Properties, Inc., A. Joseph Geist, trustee of real property of the latter company securing the payment of bond and mortgage participation certificates, petitions for an order subordinating the claims of Prudence Realization Corporation, successor of the former company, to those of other certificate holders. From an order granting the petition, respondent appeals.

Affirmed.

Before:

SWAN, CLARK and FRANK,
Circuit Judges.

MORRIS A. MARKS, of New York City (Geist & Netter, of New York City, on the brief), for petitioner-appellee.

IRVING L. SCHANZER, of New York City, for respondent-appellant.

CLARK, *Circuit Judge:*

The Prudence Company, Inc., and Prudence-Bonds Corporation, wholly owned subsidiaries of the same parent corporation—New York Investors, Inc.—were together engaged in the mortgage-guaranty business. By a common practice, Prudence would lend money on a bond and real property mortgage, which it would assign to Prudence-Bonds. The latter would place them with a public depository and would issue certificates authenticated by the depository of undivided shares of specified amounts in the bond and the mortgage. These certificates would then be sold to the public with Prudence's guarantee attached. The practice is described in *In re The Westover, Inc.*, 2 Cir., 82 F. 2d 177, and see, also, *In re Prudence Co., Inc.*, 2 Cir., 89 F. 2d 689; *In re Prudence Co., Inc.*, 2 Cir., 98 F. 2d 559, *certiorari* denied 306 U. S. 636, 59 S. Ct. 485, 83 L. Ed. 1037; *In re Prudence Bonds Corp.*, 2 Cir., 79 F. 2d 212.

This procedure was followed in connection with the issue here involved. Prudence having lent the Zo-Gale Realty Co., Inc., $480,000, the loans were consolidated in 1925 in one bond secured by mortgage of the premises at 202 Riverside Drive, New York City. Prudence immediately assigned

the bond and mortgage to Prudence-Bonds, which deposited them with Central Union Trust Company of New York and sold to the public certificates guaranteed by Prudence to the amount of $382,800. The mortgage was thereafter reduced by payment to $390,000. In 1932, Prudence repurchased two certificates in the amount of $800, and otherwise became entitled to one in the amount of $16.67. Whether claims in reorganization proceedings on these certificates totalling $816.67 and on the uncertificated balance of the loan, to wit, $7,200, stand on a parity with, or are subordinated to, the claims of general certificate holders is the question here at issue.

In proceedings for the foreclosure of a mortgage junior to the one received by Prudence, following the mortgagor's default, the property was transferred February 1, 1933, subject to Prudence's mortgage, to Amalgamated Properties, Inc., a subsidiary of Prudence. Reorganization proceedings against Prudence were begun February 1, 1935, and against Amalgamated, March 16, 1936. By an order therein of January 28, 1938, the court approved a transfer by Prudence-Bonds, also in reorganization, to the Prudence trustees of the $7,200 uncertificated portion of the Zo-Gale mortgage, in compromise of other claims. A plan for the reorganization of the Zo-Gale issue was subsequently confirmed, February 19, 1938, and pursuant thereto, title to the mortgaged property was transferred to Geist, petitioner herein, to carry out the plan.

The order of confirmation did not settle, however, the question which had been raised regarding the right of the Prudence trustees to satisfaction of their claims on a parity with other certificate holders. By Paragraph 7 thereof, Geist was forbidden to make distribution of cash or securities on account of these claims unless their right thereto had "been finally adjudicated by a court of competent jurisdiction," and by Paragraph 30, the court retained in itself jurisdiction to decide the question.

Respondent, Prudence Realization Corporation, which succeeded to the interest of the Prudence trustees following the reorganization of Prudence by an order of May 26, 1939, now opposes Geist's petition for subordination of the claims. The court below held, however, that under New York law a guarantor of mortgage certificates who also has an interest in the mortgage cannot share in the collateral until the certificate holders are paid, unless there is a clear reservation in the certificate of a right to share on a parity. Respondent has appealed from the resulting order of subordination against it.

The New York law to which the district court refers has been established in a series of recent cases dealing with the liquidation of companies engaged in the guaranteed mortgage business. *In re Union Guarantee & Mortgage Co.*, 285 N. Y. 337, 34 N. E. 2d 345; *Pink* v. *Thomas*, 282 N. Y. 10, 24 N. E. 2d 724; *In re Title & Mortgage Guaranty Co. of Sullivan County*, 275 N. Y. 347, 9 N. E. 2d 957, 115 A. L. R. 35, and other cases cited in these decisions. An important issue herein is whether this is primarily a rule of construction of the guaranty in the certificates or is a rule of administration of insolvent estates which violates bankruptcy principles of equal distribution of a bankrupt estate among creditors. If it is a rule of construction, we would follow it as we held in *In re Prudence Co., Inc.*, 2 Cir., 82 F. 2d 755, *certiorari* denied 298 U. S. 685, 56 S. Ct. 958, 80 L. Ed. 1405; and see, of course, *Erie R. Co.* v. *Tompkins*, 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, 114 A. L. R. 1487. And if we thus found the guarantee to amount to an actual agreement between two creditors that the claim of one against the debtor should be subordinated to that of the other, we should give that effect to it, as was done in *St. Louis Union Trust Co.* v. *Champion Shoe Machinery Co.*, 8 Cir., 109 F. 2d 313; *Bird & Sons Sales Corp.* v. *Tobin*, 8 Cir., 78 F. 2d 371, 100 A. L. R. 654; and *Searle* v. *Mechanics' Loan & Trust Co.*, 9 Cir., 249 F. 942, *certiorari* denied 248 U. S. 592, 39 S. Ct. 67, 63 L. Ed. 437, even though there ap-

pears to be authority contra to the effect that the enforcement of such agreements, not amounting to assignment of a claim, is entirely collateral to the interests of the estate and outside the bankruptcy power. *In re Railroad Supply Co.*, 7 Cir., 78 F. 2d 530; *In re Goodman-Kinstler Cigar Co.*, 32 A. B. R. 624; see *Nixon* v. *Michaels*, 8 Cir., 38 F. 2d 420. Where the state law determines what the actual agreement made by the parties is, and therefore the real basis of their claims in bankruptcy, it must be given effect.

If, however, the matter is one of insolvent liquidation only, we have a different situation. It is a necessary implication of the requirement of a plan of reorganization that "it is fair and equitable and does not discriminate unfairly in favor of any class of creditors," Bankruptcy Act, former §77B(f)1, as it is a corollary of the strict priorities rule of *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, 60 S. Ct. 1, that a plan may not discriminate between different members of the same class of creditors or classify creditors arbitrarily, without due regard to their economic status as defined in their respective claims. See *Southern Pacific Co.* v. *Bogert*, 250 U. S. 483, 492, 39 S. Ct. 533, 63 L. Ed. 1099; 49 Yale L. J. 881, 882; 2 Gerdes, Corporate Reorganizations, 1682; Finletter, Bankruptcy Reorganization, 465. Similarly, Bankruptcy Act, §65a, requires, in liquidation, the distribution of "dividends of an equal per centum" "on all allowed claims, except such as have priority or are secured." *Moore* v. *Bay*, 284 U. S. 4, 52 S. Ct. 3, 76 L. Ed. 133, 76 A. L. R. 1198; *Globe Bank & Trust Co.* v. *Martin*, 236 U. S. 288, 305, 35 S. Ct. 377, 59 L. Ed. 583; *Sampsell* v. *Imperial Paper & Color Corp.*, 61 S. Ct. 904, 907. The only departures made from the ordinary rule of equality are based on some very definite equity, such as fraud, *Pepper* v. *Litton*, 308 U. S. 295, 60 S. Ct. 238, 84 L. Ed. 281, mismanagement of the debtor by a parent corporation, *Taylor* v. *Standard Gas & Electric Co.*, 306 U. S. 307, 59 S. Ct. 543, 83 L. Ed. 669, or concealment of a claim to the prejudice of another creditor, *In re Bowman Hardware*

& Electric Co., 7 Cir., 67 F. 2d 792. In the absence of such an equity, subordination is not a function of the bankruptcy court. *Crowder* v. *Allen-West Commission Co.*, 8 Cir., 213 F. 177, 184; *Sampsell* v. *Imperial Paper & Color Corp., supra; cf. Moise* v. *Scheibel*, 8 Cir., 245 F. 546.

Notwithstanding the antithesis thus stated, the question might still remain somewhat more extensive than whether the New York rule is a mere rule of interpretation. For if it is a rule of law, but one attributing a certain legal result to a contract, that result must still be the basis of the bankruptcy claim—just as, for example, a New York contract of insurance must legally incorporate in itself provisions which may be directly opposed to the parties' actual intent. *American Lumbermen's Mut. Cas. Co.* v. *Timms & Howard, Inc.*, 2 Cir., 108 F. 2d 497, 502. It is still the difference between finding out what the contract claim is as opposed to adjusting priorities among ascertained claims. But, however far the answer to such a question might take us, we need not determine it here, for the New York decisions emphasize that it is the intent of the parties which they are seeking to ascertain with the aid of a "presumption of intent derived from the guaranty of the assignor." The language just quoted is from *In re Title & Mortgage Guaranty Co. of Sullivan County, supra*, where the present Chief Judge has made the most extensive analysis of the subject of any of the cases and where he discusses not merely New York, but general, precedents. He finds that the rule "is supported by the weight of authority in this and other jurisdictions and produces an equitable result in accordance with the intent of the parties," that "the decisive test in every case is the intention of the parties, either as actually expressed, or as derived from the natural equity of the situation," and that "a presumption of such intent is derived from special equities," of which the guaranty seems to be the one most noted. 275 N. Y. 353-355. In thus stating the basis of the rule he expressly eliminates "avoidance of

circuity of action" as its basis in this State; and he holds that the mere assignment of part of the mortgage without any guaranty is insufficient to raise a presumption against parity, citing *Title Guarantee & Trust Co.* v. *Mortgage Commission,* 273 N. Y. 415, 428, 7 N. E. 2d 841, 847, where such an assignment was held to permit the assignor to share *pro rata* with the assignee in the proceeds of insufficient surety. The most recent cases have followed the same principle; indeed, in the latest case of all, *In re Union Guarantee & Mortgage Co., supra,* certain language of the depository agreement was assumed to be adequate to achieve such parity but for the fact that the guarantor had cancelled its acquired certificates and had not issued others in place of them.

There is considerable authority in other jurisdictions to similar effect. *In re Phillippi,* 329 Pa. 581, 198 A. 16; *Appeal of Fourth Nat. Bank,* 123 Pa. 473, 16 A. 779; *Donley* v. *Hays,* 17 S. & R., Pa., 400; *Worrall's Appeal,* 41 Pa. 524; *Fidelity Trust Co.* v. *Orr,* 154 Tenn. 538, 289 S. W. 500; and see, also, *Whitehead* v. *Morrill,* 108 N. C. 65, 12 S. E. 894; *Cannon* v. *McDaniel,* 46 Tex. 303; *Dixon* v. *Clayville,* 44 Md. 573. The leading authority to the contrary is *Kelly* v. *Middlesex Title Guarantee & Trust Co.,* 115 N. J. Eq. 592, 171 A. 823, affirmed 116 N. J. Eq. 574, 174 A. 706, much relied on by respondent herein. The reasons assigned for the rule have varied between the effect of the guaranty as evidence of an intent to grant the assignees priority, as in the Pennsylvania and Tennessee cases cited, or, as in *Dixon* v. *Clayville* and apparently the two cases cited before it, to avoid a circuity of action in suits by the general creditors against the guarantor—a reason, as is pointed out in the *Kelly* case, which loses its force where the guarantor is insolvent. A vigorous criticism of the rule as applied to an insolvent assignor appears in 47 Yale L. J. 480-483, where it is pointed out that the rule may give the assignees a preference at the expense of unsecured creditors, and, in the case of a large holding of a single issue, prejudice other

customers of the assignor in favor of the holders of this particular issue. Compare, also, 37 Col. L. Rev. 1010; 34 Col. L. Rev. 663, 678; 14 N. Y. U. L. Q. Rev. 259; 19 R. C. L. 659, 660. In these comments it appears to be assumed that the rule is one of intent or construction of the guaranty.

Whether or not we might quarrel with the rule as an original or a general proposition, we see no occasion to do so here. Creditors of different New York mortgage-guaranty companies ought to receive similar treatment, without respect to the tribunal in which liquidation occurs, for certainly their respective investments were made under substantially identical conditions. Moreover, there appear to be no particular equities in favor of either the original guarantor or those who claim through it, including its successor, the respondent herein, which took with full notice of the situation from the reorganization proceedings generally and especially in view of the explicit reservation of the question in the confirmation of the debtor's reorganization. After all, all parties to these proceedings, guarantor, mortgagee, and debtor, are interconnected companies; and as a matter of practical equity so far as the public purchasers of certificates are concerned, it is only just that their mutual claims among each other should be subordinated until the claims of their customers have been satisfied. Moreover, the wording of the contracts here is such as to indicate an intent that the guarantor should not have parity with the others. For the agreement with Prudence-Bonds provides that it "may for its own corporate account, be the holder or pledgee of similar shares in said bond and mortgage," whereas in Prudence's guaranty such a provision is almost pointedly lacking. Under *Pink* v. *Thomas, supra,* an actual agreement against parity might well be found.

A final question arises as to the claim on the uncertificated indebtedness of $7,200, for that, at the time of the debtor's bankruptcy, was nominally in the name of Prudence-Bonds, which, in the light of the agreement just

quoted, as well as *Title Guarantee & Trust Co.* v. *Mortgage Commission, supra*, would itself be entitled to share on a parity with the certificate holders, since it was not a guarantor. But the record shows without dispute that Prudence-Bonds when it took the original assignment from Prudence did not give any money value for the bond and mortgage and could not be expected to, as it had no such assets as would justify a loan in its own right of this amount. Compare *In re The Westover, Inc., supra; In re Prudence Bonds Corp., supra.* And later collections of interest applicable to this uncertificated indebtedness went to Prudence. On the basis of such facts appearing of record the court below held that Prudence was the actual and equitable owner throughout, and hence the New York rule was applicable. We think this conclusion sound and in accordance with the undoubted realities of the relations between the parties here. On this basis both the uncertificated portion of the indebtedness and the certificates bought by Prudence prior to any of the reorganization proceedings were properly declared subordinate to the claims of the public certificate holders.

Affirmed.

FRANK, *Circuit Judge,* dissents with opinion.

FRANK, *C. J.*, dissenting:

There are two factual aspects of this case to which, I think, the majority has given insufficient attention:

(1) Prudence, the guarantor, itself is bankrupt. Its creditors are all general creditors, i.e., holders of certificates of several different issues (including the Zo-Gale issue) which Prudence had guaranteed, their claims all being based on the obligations of Prudence on those guarantees. Among the assets of the Prudence estate are the Zo-Gale certificates held by Prudence. The majority, by subordinating Prudence's claim in the Amalgamated proceedings, is thus preferring the claims of one group of Prudence's general creditors—the holders of the Zo-Gale certificates—to those of Prudence's other general creditors, i.e., the holders of other certificates guaranteed by Prudence, by giving assets to the Zo-Gale holders which would otherwise be divided among all of Prudence's general creditors.

(2) If the certificates which are the basis of Prudence's claim against Amalgamated had not been repurchased from their holders by Prudence,[1] or if certificates had been issued against the uncertificated interest here involved and had been sold to the public, the holders of those certificates could have proved them, in the reorganization of Amalgamated, on a parity with the Zo-Gale certificates which are now, in fact, so held by the public. It is only because of the fortuitous circumstances that Prudence, under conditions which no one even intimates were improper, repurchased the certificates and failed to sell, of its own choice, the uncertificated interest, that the public holders of the Zo-Gale issue claim that they are entitled to a larger share of the

1 Or if they had again been resold, before the reorganization, to the public.

available assets than they would have received if all the certificates were publicly owned.

Those facts are, to my mind, controlling: As the majority points out, the usual federal rule of bankruptcy administration would require that Amalgamated's assets should be equitably distributed, without such a preference, among all claimants, Prudence[2] as well as the public certificate holders. I am satisfied to take as my text the majority's words: "The only departures made from the ordinary rule of equality are based on some very definite equity. • • • In the absence of such an equity, subordination is not a function of the bankruptcy court." I search in vain both the record and the majority opinion to find any evidence of such an equity. I find, rather, that the preference is markedly inequitable. There is also the striking fact that the entire case for subordination rests upon the mere accidental repurchase of the certificates; because of this adventitious fact, subordination is a windfall to the other holders of the Zo-Gale certificates, and the other creditors of Prudence—which, so far as appears, retained the uncertificated interest and repurchased the certificates solely as an investment, and held them in place of either cash or other securities—find the assets of Prudence depleted.

The only equity suggested by the majority opinion to justify the preference is that the companies are interconnected so that "it is only just that their mutual claims among each other should be subordinated until the claims of their customers have been satisfied." I am unable to follow that reasoning. This is not at all a case of a parent company asserting a creditor claim against an insolvent subsidiary which it had organized and/or operated for its

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2 Hereafter I shall, for convenience, treat the uncertificated portion of the mortgage as identical with the repurchased certificates; as the majority points out, Prudence was the true owner of both.

own benefit, as in *Taylor* v. *Standard Gas & Electric Co.*, 306 U. S. 307 and related cases.[3] There is no suggestion that Prudence interfered in the affairs of Zo-Gale Realty Company or mismanaged it, but merely made it, an autonomous entity, a loan for which Prudence received a bond and mortgage, some participation certificates in which Prudence sold to others, with a guarantee.

The majority opinion makes an additional argument: Appellant, it says, "took with full notice of the situation" because the issue of subordination was reserved in the Zo-Gale reorganization proceedings. But that sort of notice is inefficacious to create equities: Appellant represents the interests of Prudence's creditors; it was created long after they became creditors; they became creditors without any such notice; that notice served merely to keep open for future decision the question, first raised in the Zo-Gale proceedings, of whether, because of facts previously occurring, there should be a subordination.

Since I am unable to find "some very definite equity" in favor of subordination—in the absence of which, as the majority opinion says, "subordination is not a function of the bankruptcy court"—I would follow the normal principle of bankruptcy administration, that "equality is equity". So far as the New York rule applies to a situation where the guarantor is itself solvent, I regard it as both fair and practicable, and see no reason why the federal courts should not adopt it.[4] But *it becomes a totally different rule when, as here, the guarantor itself is a bankrupt; then the problem which confronts the federal courts is one of equitable*

3 Were the facts of this case such as to bring it within the general outlines of the rule of the *Taylor* case, *supra*, we would be obliged to consider the significance of the cautionary comments in *Consolidated Rock Products Co.* v. *DuBois*, —— U. S. —— (March 3, 1941).

4 In such a situation, the federal courts are bound by the decisions of the New York courts as to whether language in the contract has the effect of overcoming the New York rule as to subordination, for such decisions relate to the intention of the parties to the contract.

distribution, under the Bankruptcy Act, of the insufficient proceeds of a guaranteed obligation among all the guarantor's creditors, including the assignees of a portion of the guaranteed obligation.

The majority opinion seems to imply, however, that, under *Erie* v. *Tompkins*, 304 U. S. 64, we are not free to apply the rules generally applicable in federal bankruptcy decisions because subordination is required by the New York decisions as to the *intention of the parties* to such contracts. But I do not read the New York decisions as holding that subordination, in such a case as this, results from the intention of the parties. As I understand those decisions, they say that, in such a case, subordination is an equitable rule of administration in the distribution of the primary obligor's assets among an insolvent guarantor and its assignee-creditors. The preference is granted even when, as in the case at bar, there is no evidence of any kind—in the verbiage of the contract or otherwise—that the parties had any actual intention to create or not to create one.[5] Absent any evidence of such an intent, the New York Court, nevertheless, sustains such a preference as against the other creditors of the insolvent guarantor on the basis of what that Court calls "the existence of special equities" arising solely from the guaranty. *Matter of Title & Mortgage Guaranty Co.*, 275 N. Y. 347, 355; *Title Guarantee & Trust Co.* v. *Mortgage Commission*, 273 N. Y. 415, 426; *New York Trust Company* v. *United Equities*, N. Y. L. Journal, June 12, 1941. Reference is also made to "the implied or actual intent of the parties;" *Pink* v. *Thomas*, 282 N. Y. 10, 15; *Granger* v. *Couch*, 86 N. Y. 484; "implied" is significantly differentiated from "actual" intent and thus means intent "implied in law", i.e., not intent at all. And

5 In some of the cases decided by the New York court, it found language in the contract showing an actual intention to create a preference. But in the case at bar there is not a vestige of such language.

the same is true of the locution in some of the above cases as to a "presumption of intent" as distinguished from the "actual intent." In *Pink* v. *Thomas, supra* (p. 12), the court states the basis of the rule thus: "Having guaranteed the payment of the certificates it would be highly *inequitable* to permit it (the guarantor) to step in and divert part of the security available to pay such certificate holders whom it had expressly guaranteed should be paid;" the guarantor may hold on a parity, if the contract clearly shows that the parties intended it; but "such an *inequitable result* could be accomplished if the language used was so clear and unmistakable that the courts would be compelled to give effect to the intent of the parties as expressed in the writing. Otherwise the *equitable rule* should apply."[6] That is not the verbiage which the New York court would employ if it were determining that the parties had an actual intention, expressed in their contract, to create a preference; but it is verbiage appropriate in spelling out a rule of insolvency administration. And my brother judges concede that *Erie* v. *Tompkins* does not require us to adopt such a rule.

A contrary argument (implied in the majority opinion here) runs thus: If a contract relating to the sale of a guaranteed obligation contains an express provision showing a clear intention to negate the New York subordination rule, such a provision is given effect by the New York courts; consequently the failure to insert such an express negating provision in the contract is the equivalent of intentionally inserting an express provision adopting the New York rule of administration of the guarantor's insolvent estate; therefore, where, as here, no such negating clause was included, we are not substituting the New York rule of insolvency distribution for the federal bankruptcy rule, but are compelled to apply an actual provision of the contract which is

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6 Italics added.

implied in fact. That argument proves too much; it amounts to saying that parties to a contract are always to be deemed actually to intend to include in their contract any rule of law which they could, by contract, nullify, but which they do not. Such an argument, too, rests on a fiction; and fictions should be sparingly employed and never utilized to bring about unjust results. *United States* v. *Bags of Coffee,* 8 Cranch. 398, 415; *Helvering* v. *Stockholm Bank,* 293 U. S. 84, 82; *Curry* v. *McCanless,* 307 U. S. 357, 374.

Even if the majority opinion were correct in suggesting that the New York courts have said that their rule is not one of insolvency administration, but one of interpretation of the intention of parties to this kind of contract, I would still dissent. For I cannot believe that what, by its nature, is a rule of administration of insolvent estates can be transformed into such a rule of interpretation—and that, therefore, it becomes binding on the federal courts merely because of the label attached to the rule by the State Court. To illustrate: In applying the doctrine of *Taylor* v. *Standard Gas & Electric Co., supra,* the Supreme Court did not look to the decisions of the State Court. If the courts of that State were hostile to the rule of the *Taylor* case, and (taking a hint from the majority opinion in the instant case) were to say that it construes contracts made by creditors with a subsidiary corporation as showing an intention to exclude the rule of the *Taylor* case unless expressly contracted for, I doubt whether the Supreme Court would, simply on that account, refuse to apply that rule. In other words, I doubt whether *Erie* v. *Tompkins* is so cannibalistic.

And my doubt is especially strong where the rule of the State Court is squarely contrary to the federal rule under the federal Bankruptcy statute and where federal jurisdiction is founded upon that statute. If the majority opinion is correct, *Erie* v. *Tompkins* is likely soon to break up such uniformity of federal decisions as now exists relative

to federal bankruptcy administration. What will then become of the provisions of the Constitution which authorizes Congress to enact "*uniform* laws on the subject of bankruptcies throughout the United States?" Surely respect for State's rights should not be carried that far. It has never suggested that statutes enacted under the interstate commerce or admiralty clauses must be given varying applications responsive to divergent State decisions; yet those clauses of the Constitution, unlike that relating to bankruptcies, make no explicit mention of laws which are to be "uniform * * * throughout the United States." *Erie* v. *Tompkins*, according to some of the Justices who joined in it, repudiated the rule of *Swift* v. *Tyson* on the ground that rule, in so far as it permitted the federal courts to ignore State court decisions, was unconstitutional; but no one would venture to deny to Congress the power to provide that, generally, uniformity and not variety should govern in bankruptcy; and such congressional intention should be presumed in the light of the express wording of the bankruptcy clause.

Related considerations are pertinent with respect to the suggestion in the majority opinion that, even if we are free to ignore the New York rule, we should not do so, since, thereby, persons in similar circumstances, *vis a vis* an insolvent guarantor, will be treated differently by State and federal tribunals. Such an argument is self-defeating: No doubt uniformity between State and federal courts is desirable; but so is nationwide uniformity of bankruptcy administration; if the majority opinion assists in establishing the first of these, it helps to destroy the second. Where a paramount public policy does not demand it, I can see no reason for our going out of our way to transplant, from the State to the federal courts, a doctrine which is so curiously lacking in logic and fairness as the New York rule of automatic subordination.

Although not considered in the majority opinion, there is this further possible argument to sustain the preference: It might conceivably be argued that the rule of the New York court had the effect of creating an equitable lien in the Zo-Gale mortgage, in favor of the public certificate holders, i.e., that, in effect, the guaranty, from its inception, gave them a first lien on that mortgage. But the New York court nowhere suggests that its rule is to be taken as creating such an equitable lien, in all likelihood because the existence of such a lien cannot be reconciled with the fact that, under the New York decisions, the guarantor, with entire legality, can destroy it at any time, by merely selling the unissued or repurchased certificates without the consent of the holders of the then outstanding publicly held certificates.[7]

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[7] Such a "lien" would not rise even to the dignity of an unrecorded chattel mortgage. It may also be noted, in passing, that the rights of the Trustees in bankruptcy of Prudence vested before Amalgamated went into bankruptcy.

Order for Mandate.

UNITED STATES CIRCUIT COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 29th day of August, one thousand nine hundred and forty-one.

Present: HON. THOMAS W. SWAN,
HON. CHARLES E. CLARK,
HON. JEROME N. FRANK, *Circuit Judges.*

IN THE MATTER
OF
THE PRUDENCE COMPANY, INC.,
Debtor,
PRUDENCE REALIZATION CORPORATION,
Appellant.

Appeal from the District Court of the United States for the Eastern District of New York.

This cause came on to be heard on the transcript of record from the District Court of the United States for the Eastern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is affirmed with costs.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

D. E. ROBERTS,
Clerk.

UNITED STATES CIRCUIT COURT OF APPEALS

Second Circuit

In the Matter

of

The Prudence Company, Inc.,

Debtor,

Prudence Realization Corporation,

Appellant.

ORDER FOR MANDATE

United States Circuit Court of Appeals
Second Circuit

Filed August 29, 1941

D. E. Roberts, Clerk.

Clerk's Certificate.

UNITED STATES OF AMERICA

SOUTHERN DISTRICT OF NEW YORK

I, D. E. ROBERTS, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify that the foregoing pages, numbered from 1 to 75, inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of

IN THE MATTER

OF

THE PRUDENCE COMPANY, INC.,
Debtor,

PRUDENCE REALIZATION CORPORATION,
Appellant.

as the same remain of record and on file in my office.

IN TESTIMONY WHEREOF, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit this seventeenth day of September, in the year of our Lord one thousand nine hundred and forty-one, and of the Independence of the said United States the one hundred and sixty-sixth.

(Seal)

D. E. ROBERTS,
Clerk.

[fol. 77] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed January 5, 1942

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Mr. Justice Roberts took no part in the consideration and decision of this application.